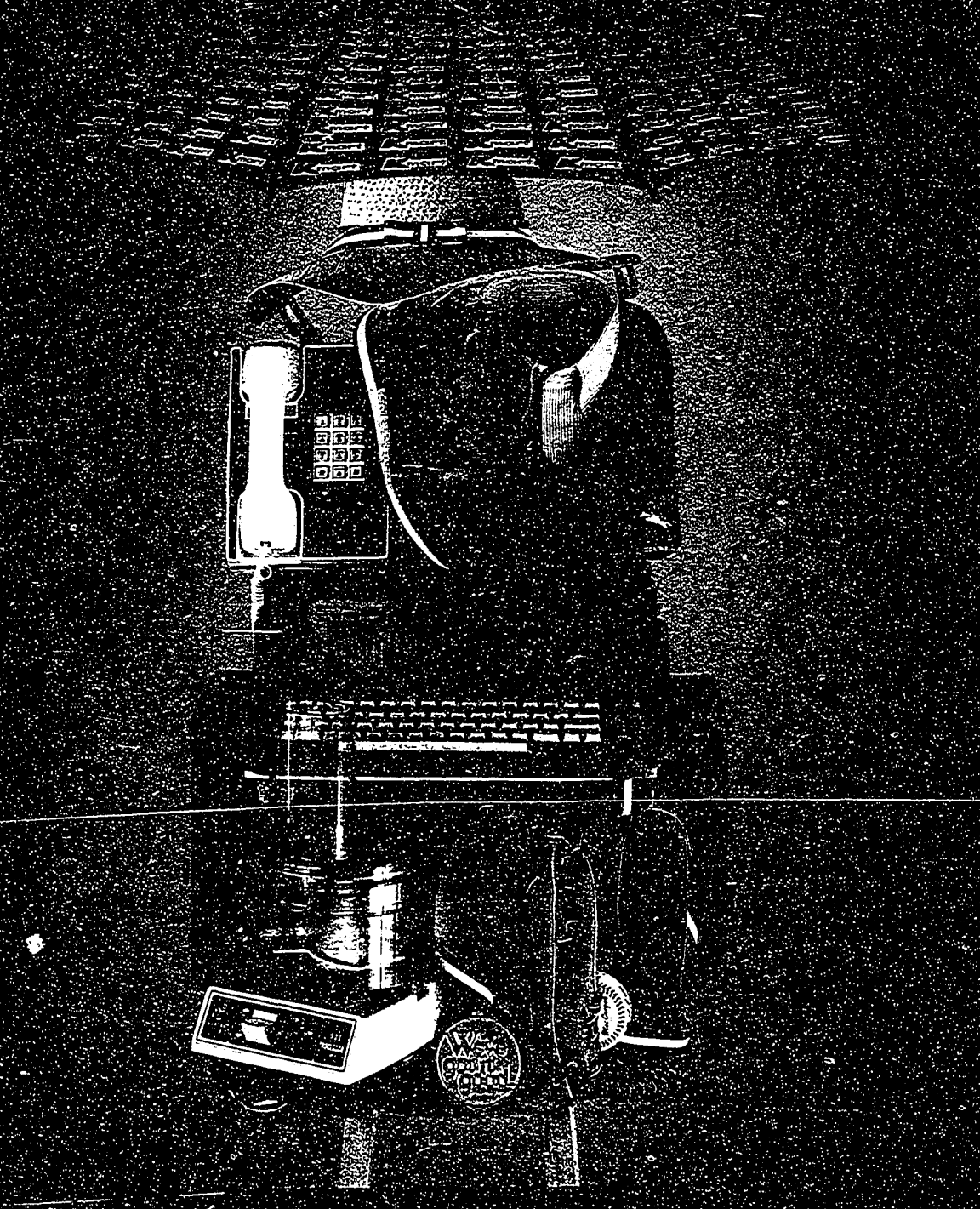


K MART CORPORATION 1983 ANNUAL REPORT



Below: Redesigned Domestic Center and apparel departments are two of many changes within K-mart stores that align product and presentation with the tastes of contemporary families. A glimpse of K-mart Corporation's new retailing approach begins on page six.



On the cover, a sample of K-mart's 1984 selection for modern families. Among the thousands of top quality products are General Electric kitchen appliances, sporting goods from Wilson and MacGregor, Vermont American tool chests, Commodore Executive 64 computers, telephones (including M&I in some stores), Trax athletic shoes, Private Club men's shirts, Steeplechase sweaters and stylish accessories.

# FINANCIAL HIGHLIGHTS

| (Millions)                                      | 1983       | 1982       |
|-------------------------------------------------|------------|------------|
| Sales                                           | \$18,597.9 | \$16,772.2 |
| Net income                                      | \$ 492.3   | \$ 261.8   |
| Earnings per common and common equivalent share | \$ 3.80    | \$ 2.06    |
| Cash dividends declared                         | \$ 135.1   | \$ 124.3   |
| Per share                                       | \$ 1.08    | \$ 1.00    |
| Employee compensation and benefits              | \$ 2,891.2 | \$ 2,781.6 |
| Per sales dollar                                | 15.55%     | 16.58%     |
| Depreciation and amortization—owned assets      | \$ 167.8   | \$ 157.4   |
| Per sales dollar                                | .90%       | .94%       |
| Property additions—owned assets                 | \$ 377.9   | \$ 306.4   |
| K mart stores                                   | 2,160      | 2,117      |
| Kresge, Jupiter and other retail units          | 387        | 452        |

## CORPORATE PROFILE

**K MART CORPORATION** is the world's second-largest retailer in sales volume. The company's principal business is general-merchandise retailing. As of January 25, 1984, the company operated 2,160 K mart discount department stores, 201 Kresge variety and Jupiter limited-line discount stores, 29 Designer Depot off-price specialty apparel stores, and a total of 157 cafeterias and other retail units in the United States, Canada and Puerto Rico.

In addition to its wholly owned subsidiaries, which are part of the general-merchandise retailing operations, the company has several important equity interests that operate in the United States and internationally. These equity interests include K mart's footwear departments in the United States, operated by the Meldisco subsidiaries of Melville Corporation, and foreign equity interests or affiliations in Australia, Mexico and Japan.

Additionally, K mart Corporation has three wholly owned subsidiaries that operate in areas other than general-merchandise retail operations. Furr's Cafeterias, Inc. and Bishop Buffets, Inc. operate chains of 117 and 30 cafeterias, respectively, in the southwestern, midwestern and western United States. Furr's and Bishop offer high-quality food at moderate prices. K mart Insurance Services, Inc. underwrites and markets insurance.

## CONTENTS

|                                                          |    |
|----------------------------------------------------------|----|
| <i>Letter to Shareholders</i>                            | 2  |
| <i>Kmart Grows with a Changing Family</i>                | 6  |
| <i>10-Year Financial Summary</i>                         | 12 |
| <i>1983 Operations and Financial Review</i>              | 14 |
| <i>Reports by Management and Independent Accountants</i> | 26 |
| <i>Financial Statements</i>                              | 27 |
| <i>Notes to Financial Statements</i>                     | 31 |
| <i>Directors, Officers and Corporate Data</i>            | 40 |

## TO OUR SHAREHOLDERS

During 1983, we told our associates and the financial community that this would be the year for K mart to reap a harvest of benefits from the seeds of change we had planted over the preceding three years. Actual results for 1983 support that initial optimism. Net earnings for the year were \$492.3 million, an increase of 88.0% from the \$261.8 million generated in 1982. Sales for the full year were \$18.6 billion, an increase of 10.9% over 1982. Earnings per common and common equivalent share were \$3.80 in 1983, compared with \$2.06 in 1982.

In the fourth quarter of 1983, sales rose 10.0% to \$5.7 billion. Net income set a record at \$248.6 million, an increase of 50.4% over the record level achieved in 1982. Earnings per common and common equivalent share for the fourth quarter were \$1.91, compared with \$1.28 in 1982.

Behind these operating results was a significant reduction in the cost of merchandise sold (including buying and occupancy costs) as a percentage of sales. In 1983, the ratio was 72.3%, compared with 73.3% in 1982. Equally important was the reduction in selling, general and administrative expenses (including advertising) as a percentage of sales. In 1983, this ratio was 23.1%, while in 1982 it was 23.9%. These improvements led to a significant increase in the ratio of net income to sales from 1.6% in 1982 to 2.6% in 1983. Consequently, return on beginning assets increased from 3.9% in 1982 to 6.7% in 1983, the highest level achieved since 1979. Parallel to the improvement in return on assets, return on shareholders' beginning equity reached 18.9%

in 1983, compared with 10.7% in 1982.

While the results of 1983 are encouraging, they are only the first signs of the economic viability of the new "K mart for the '80s" that we have been developing and refining since the beginning of this decade.

Given the unparalleled level of effort, activity and change in 1983, it is difficult to single out the most important events of the year. Certainly one key area was the response of the American consumer to the introduction of name-brand apparel in our K mart merchandise assortments. This, coupled with the significant operational improvements from the integration of men's and boys' merchandise into the K mart Apparel Corp. system, provided outstanding sales and profits for the apparel subsidiary. Further, the new approach to layout and design in our K mart apparel departments has significantly increased apparel sales.

During 1983, K mart also implemented a variety of changes in other departments of K mart stores. Among these were new "soft goods for the home" departments offering high-fashion bed and bath merchandise. Current plans call for the addition of up to 500 of these units in 1984. More than 500 Kitchen Korner units were put in place in 1983 with plans to expand this concept to 650 more K mart stores by the end of 1984. Home Electronic Centers were installed in 715 K marts by the end of 1983, and more than 40 Home Care Centers were added in K mart stores.

Along with these restructured departments were refinements to merchandise in book departments, stationery, health food

and nutrition, party goods, prestige cosmetics and many other categories.

Currently, 126 regional teams are involved in our accelerated effort to implement the new K mart around the country. We have also added executive staff to our headquarters and regional offices to ensure timely completion of this program. The commitment in 1984 to these new projects inside existing stores accounts for approximately two-thirds of the total capital expenditures budget of some \$400 million. Over the next five years, our capital commitment will exceed \$2.0 billion. In 1983, 71 K mart stores were opened in the U.S., Canada and Puerto Rico. In 1984, we anticipate opening approximately 30 to 35 additional K marts.

Our 1984 strategy for adapting existing K marts to the concept of the '80s is two-pronged. In part, we will concentrate on key major markets in which all stores will be thoroughly updated. These markets include Atlanta, Denver, Chicago, Detroit and Buffalo. At the same time, we have targeted key locations in smaller markets, particularly in areas of rapid growth and significant new competition, for many of our new programs. In these smaller communities, our stores are generally quite new. Our program places heavy emphasis on broadening the merchandise assortments by using cubic space much more effectively. In test stores where this was accomplished in 1983, sales improvements were very substantial.

In addition to the development of K mart assortments and presentation for the '80s, we have also reassessed the role of

K mart in the community. In the 1960s and early 1970s, we felt strongly that K mart could best serve the community by offering goods and services that represented high value to our customers. Today we must do more. We realize that it is important to be active in the community, both with talents and financial resources. Consequently, we have steadily built our involvement in local United Way campaigns while increasing our financial commitments to these communities. In 1983, we also increased the budgets that local store managers can use to benefit the community and gave these managers greater autonomy in determining how best to invest those dollars. We have clarified that we would most like to aid programs that blend with K mart's dedication to the support and growth of the American family. Specific activities could be as varied as providing our parking lot for a Boy Scout car wash, permitting a bake sale on our sidewalk to raise funds for the handicapped or placing canisters inside our stores to support the United States Olympic Team.

Our corporate-level commitment to the external community has also expanded. For example, we contributed \$1.0 million to the 1984 U.S. Olympic Committee, approximately one-tenth of which was raised through customers in a canister campaign last fall.

Equally important to the future growth of K mart Corporation is the aggressive pace of new business development outside of the K mart discount department store. In 1983, the company acquired Bishop Buffets, Inc., a cafeteria chain based in Cedar Rapids, Iowa.

This latest acquisition in the food-away-from-home business fits well both geographically and philosophically with Furr's Cafeterias, Inc., which we acquired in 1980. In 1983, Furr's continued its rapid expansion program with the opening of 20 new units, including its first cafeteria in California.

**T**he Designer Depot off-price apparel concept initiated by K mart in December 1982 grew to 29 stores by the end of 1983. There are now seven units in Michigan, six in Ohio, five in Pennsylvania, three in Kentucky and two each in Delaware, California, Indiana and Illinois. We anticipate opening approximately 30 additional Designer Depots in 1984, with emphasis on filling in various markets we entered in 1983. The development of Designer Depot into a full-fledged business has proceeded rapidly. Key events were the acquisition of a 472,000-square-foot distribution center in Pennsylvania to serve the expanding network of stores and expansion of the original core management group for Designer Depot.

In November 1983, we opened a variation of Designer Depot called Garment Rack. This retail store takes advantage of certain "special buy" opportunities for apparel that we would not sell in Designer Depots.

**A**nother experiment launched in 1983 was our first Accents off-price home fashions and housewares store. Accents features top-of-the-line china, crystal and household accessories at competitive discount prices. Also sold is a broad assortment of middle-priced housewares at discount prices. While the initial intent of Accents was a one-store experiment, our

success has prompted us to consider a modest expansion of this new retailing vehicle in 1984.

In 1983, we also capitalized on the significant growth opportunities in financial services. In the Dallas-Fort Worth area we now have 22 insurance centers offering a full line of life, health and accident insurance policies through K mart Insurance Services, Inc., our wholly owned insurance company. There are also five of these units in the state of Florida. In conjunction with this insurance marketing operation, three K mart stores in Florida began a program with Standard Federal Savings and Loan Association, which makes available attractive interest rates on certificates of deposit and money market deposit accounts.

**S**ubsequent to the end of fiscal 1983, K mart Corporation and Hechinger Company of Washington, D.C., began a joint venture to develop large, free-standing warehouse-style home center operations. While it is too early to elaborate on the objectives of this new retailing venture, we are confident that the combined talent and resources of these two companies provide the basis for a highly competitive entry into the rapidly growing discount home improvement specialty business.

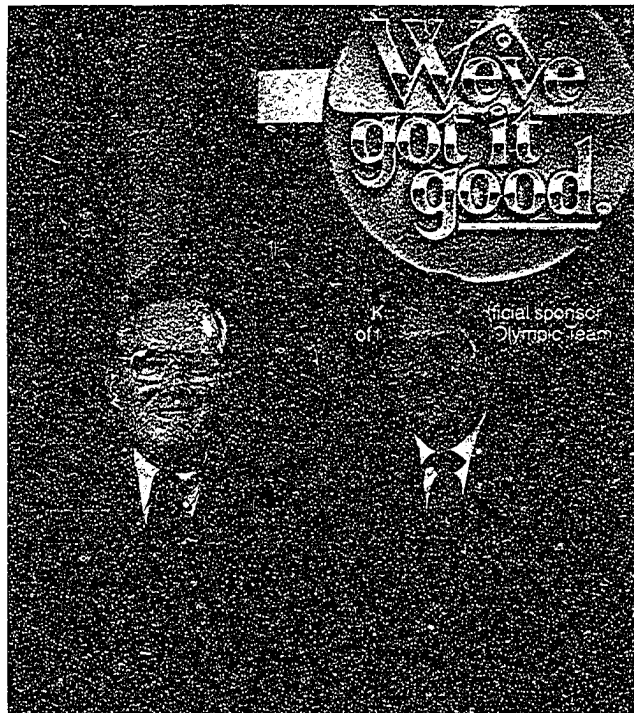
These new business developments represent K mart's initial efforts to develop new growth vehicles for our shareholders. We are actively looking at a variety of new opportunities. Areas of particular, though not exclusive, interest include additional financial services, food-away-from-home and specialty discount retail businesses.

Since the beginning of this decade, we have come a long way in developing an organization that is flexible, energetic and creative. Our goal for the balance of the 1980s and beyond is to be a dominant competitive force in the American economy.

The K mart discount department store in the United States and Canada will continue to offer the best values on a wide assortment of merchandise demanded by our customers. We will continually seek new merchandise to add to our selections. We will not hesitate to eliminate items, categories or departments when lower consumer demand necessitates that action, regardless of how successful we may have been in selling those product categories in the past. We are fully committed to offering our customers an atmosphere of friendly and helpful service. To accomplish this task, we must sustain our highly energetic, well-motivated cadre of managers, assistant managers and store associates. Accordingly, we will maintain a high level of recognition for outstanding performance and intensive training to broaden each K mart associate's responsibilities and talents.

Finally, we recognize that we must pursue new avenues of growth that lend themselves to the management and financial resources of the corporation and K mart's fine reputation with our customers, our suppliers and the financial community. We believe our efforts will provide superior returns for our shareholders.

March 7, 1984



*B.M. Fauber*      *S.G. Leftwich*

B.M. Fauber  
*Chairman of the Board*

S. G. Leftwich  
*President*

## K MART GROWS WITH A CHANGING FAMILY

America's family is changing, and K mart is changing with it.

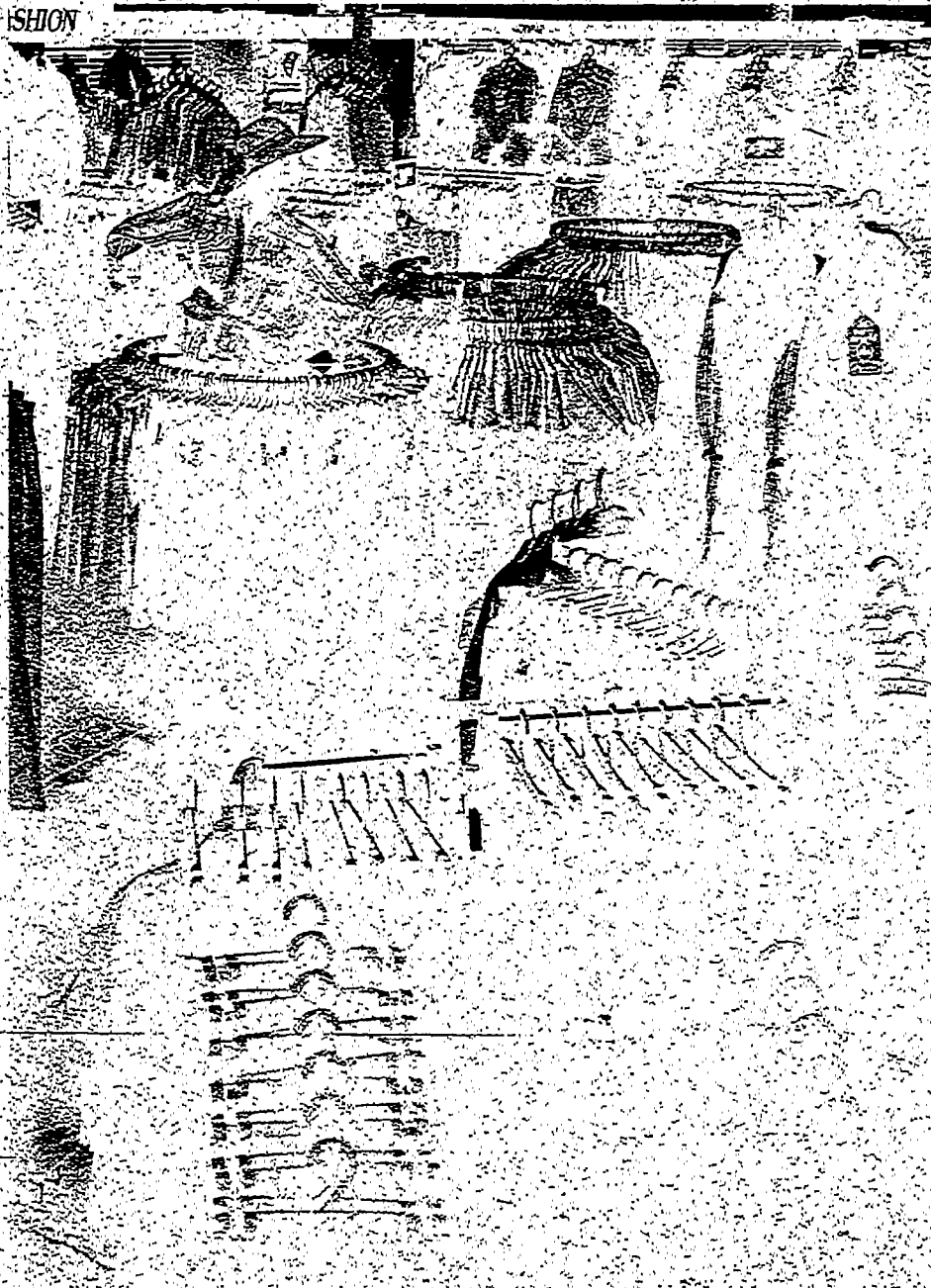
When the first K mart store opened two decades ago, the American family had two young parents, two or more school-age children and one income.

But there is no "typical" family today. More and more common are couples with one child or without children, older couples whose children no longer live at home, single parents and one-person households.

Families now are often forming later in life than in the early 1960s. These older couples, themselves products of a postwar baby boom, could generate a smaller-scale surge in the birth rate during this decade.



SHION



Diverse as they are, today's families frequently have common lifestyles and values. For example, half of all adult women now work outside the home. Also of note is that K mart customers, who span all economic levels, widely value home ownership. And while incomes may be larger than they were in years past, most families remain conscious of inflation and taxes.

Consumers today are well-educated and informed. They want good value—and they know it when they see it. Price remains a key consideration, but the consumer's new definition of value includes quality as well as price.

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**A**nticipating the needs and preferences of all families, K mart is refining its selection while insisting on standards of quality, durability and discount prices. Reflecting the trust that families place in brand names, K mart merchandise today includes a strong representation of national brands.

K mart has reappportioned and redesigned the space devoted to each product category that families want today and will seek tomorrow. Contemporary layouts and lighting emphasize the key merchandise in a tasteful and appealing fashion.

Among the major innovations are Home Care Centers, now in more than 400 K mart stores, which appeal to economy-minded families that maintain their own homes. Home Care Center merchandise has been expanded to attract the growing market of do-it-yourselfers. In 1984, Home Care Centers

## HOMECARE CENTER



## CONTEMPORARY LIVING





*Stocked with simple saucepans and sophisticated gadgetry, Kitchen Korners please all palates.*

will be introduced in 125 more K marts.

Other home-related goods are also receiving emphasis in K mart stores. Domestic Centers, for example, now provide upgraded soft goods for bed, bath and table at affordable prices in 91 K marts. Up to 500 Domestic Centers will be added in 1984.

Kitchen Korners in more than 500 K marts offer an abundance of attractive and functional goods for cooking, entertaining and gift-giving. The varied merchandise appeals to gourmet cooks as well as frozen-dinner chefs. Kitchen Korners are slated for some 650 more K marts in 1984.

Home electronics departments bring current technology within reach of K mart customers at competitive prices. Home computers



and software anchor the department, which also sells video cassette recorders and tapes, telephone equipment, name-brand audio products, microwave ovens and televisions. Some 750 home electronics departments will be added in 1984 to the current base of 715.

Among other developments in selected K marts are nutrition and health food departments, wicker shops, unfinished furniture, expanded book departments and upgraded stationery and greeting card departments.

In apparel, the emphasis is on style and durability. Familiar names are represented and displayed prominently, and private labels that meet or surpass quality standards of name-brand equivalents have a strong presence as well.





Fashion and extended wearability also characterize Designer Depot, the new retail specialty division of K mart Corporation. Designer Depot provides famous-name apparel for entire families. Most units also offer brand-name shoes, and some have bed and bath departments.

Designer Depot merchandise, all first-quality, sells for 20% to 70% less than prices normally found in department stores.

Since 1962, K mart has been known for serving modern families. Through its ongoing refinement of product and presentation, K mart also intends to have the right merchandise for the families of tomorrow.

*Designer Depots provide name-brand career wear and casual attire for today's parents and fun fashions for their children.*

## EARNINGS PER COMMON AND COMMON EQUIVALENT SHARE AND CASH DIVIDENDS DECLARED PER SHARE

(Dollars)

\$4.00

3.50

3.00

2.50

2.00

1.50

1.00

.50

'74 '75 '76 '77 '78 '79 '80 '81 '82 '83



EARNINGS PER COMMON AND COMMON EQUIVALENT SHARE



CASH DIVIDENDS DECLARED PER SHARE

## RETURN ON ASSETS (BEGINNING)

8%

7

6

5

4

3

2

1

'74 '75 '76 '77 '78 '79 '80 '81 '82 '83

## 10-YEAR FINANCIAL SUMMARY

### SUMMARY OF OPERATIONS (Millions)

Sales

Licensee fees and other income

Cost of merchandise sold

Selling, general and administrative expenses

Interest expense-net

Debt

Capital leases

Income before estimated income taxes

Income from retail operations

Net income

### PER SHARE DATA (Dollars)

Earnings per common and common equivalent share

Cash dividends declared

Book value

### FINANCIAL DATA (Millions)

Working capital

Total assets

Long-term obligations

Debt

Capital leases

Average shares outstanding

### FINANCIAL RATIOS

Return on sales

Income before estimated income taxes

Income from retail operations

Net income

Return on assets (beginning)

Debt and equivalent as a % of total capitalization

Return on shareholders' equity (beginning)

Employee compensation and benefits, per sales dollar

Current ratio

| 1983     | 1982     | 1981     | 1980     | 1979     | 1978     | 1977    | 1976    | 1975    | 1974    |
|----------|----------|----------|----------|----------|----------|---------|---------|---------|---------|
| \$18,598 | \$16,772 | \$16,527 | \$14,204 | \$12,731 | \$11,696 | \$9,941 | \$8,382 | \$6,798 | \$5,536 |
| 243      | 214      | 196      | 175      | 165      | 139      | 123     | 102     | 86      | 76      |
| 13,447   | 12,299   | 12,360   | 10,417   | 9,283    | 8,566    | 7,299   | 6,147   | 4,991   | 4,197   |
| 4,305    | 4,049    | 3,810    | 3,326    | 2,839    | 2,503    | 2,085   | 1,750   | 1,409   | 1,147   |
| 46       | 43       | 69       | 65       | 29       | 17       | 12      | 8       | 12      | 21      |
| 189      | 176      | 161      | 135      | 120      | 115      | 104     | 95      | 77      | 63      |
| \$ 854   | \$ 419   | \$ 323   | \$ 436   | \$ 625   | \$ 634   | \$ 564  | \$ 484  | \$ 395  | \$ 184  |
| \$ 487   | \$ 257   | \$ 216   | \$ 256   | \$ 355   | \$ 342   | \$ 296  | \$ 261  | \$ 204  | \$ 99   |
| \$ 492   | \$ 262   | \$ 220   | \$ 261   | \$ 358   | \$ 344   | \$ 298  | \$ 262  | \$ 196  | \$ 102  |
| \$ 3.80  | \$ 2.06  | \$ 1.75  | \$ 2.07  | \$ 2.84  | \$ 2.74  | \$ 2.39 | \$ 2.11 | \$ 1.61 | \$ .85  |
| \$ 1.08  | \$ 1.00  | \$ .96   | \$ .92   | \$ .84   | \$ .72   | \$ .56  | \$ .32  | \$ .24  | \$ .22  |
| \$ 23.35 | \$ 20.89 | \$ 19.81 | \$ 18.99 | \$ 17.79 | \$ 15.68 | \$13.56 | \$11.62 | \$ 9.69 | \$ 8.25 |
| \$ 2,268 | \$ 1,827 | \$ 1,473 | \$ 1,552 | \$ 1,403 | \$ 1,308 | \$1,231 | \$1,074 | \$ 904  | \$ 773  |
| \$ 8,183 | \$ 7,344 | \$ 6,657 | \$ 6,089 | \$ 5,635 | \$ 4,836 | \$4,489 | \$3,983 | \$3,336 | \$2,719 |
| \$ 711   | \$ 596   | \$ 415   | \$ 419   | \$ 209   | \$ 209   | \$ 211  | \$ 211  | \$ 210  | \$ 212  |
| \$ 1,822 | \$ 1,824 | \$ 1,752 | \$ 1,618 | \$ 1,422 | \$ 1,294 | \$1,266 | \$1,155 | \$ 989  | \$ 846  |
| 125      | 124      | 124      | 123      | 123      | 122      | 122     | 121     | 121     | 120     |
| 4.6%     | 2.5%     | 2.0%     | 3.1%     | 4.9%     | 5.4%     | 5.7%    | 5.8%    | 5.8%    | 3.3%    |
| 2.6%     | 1.5%     | 1.3%     | 1.8%     | 2.8%     | 2.9%     | 3.0%    | 3.1%    | 3.0%    | 1.8%    |
| 2.6%     | 1.6%     | 1.3%     | 1.8%     | 2.8%     | 2.9%     | 3.0%    | 3.1%    | 2.9%    | 1.8%    |
| 6.7%     | 3.9%     | 3.6%     | 4.6%     | 7.4%     | 7.7%     | 7.5%    | 7.8%    | 7.2%    | 4.3%    |
| 47.0%    | 48.7%    | 47.2%    | 46.8%    | 43.1%    | 44.4%    | 47.7%   | 49.6%   | 51.0%   | 51.9%   |
| 18.9%    | 10.7%    | 9.4%     | 11.9%    | 18.7%    | 20.8%    | 21.1%   | 22.4%   | 19.8%   | 11.3%   |
| 15.6%    | 16.6%    | 15.8%    | 16.0%    | 15.2%    | 14.6%    | 14.3%   | 14.3%   | 14.3%   | 14.5%   |
| 1.9      | 1.8      | 1.8      | 2.0      | 1.8      | 1.9      | 1.9     | 1.9     | 2.0     | 2.2     |

# 1983 OPERATIONS AND FINANCIAL REVIEW

## *A Year of Record Earnings*

For K mart Corporation, 1983 was a very successful year. The company reported record earnings for the year, as well as in three of the year's quarters. Although the economic recovery provided impetus for the company's results, record sales and net income levels could not have been achieved without the strategies implemented by the company over the past three years. During the adverse economic conditions of the early 1980s, K mart assessed and improved its merchandising strategies, operations and electronic information systems. Accordingly, a number of programs and strategies were developed to meet the needs and preferences of the consumer of the 1980s. These programs and strategies have resulted in:

- Better utilization of resources in existing K mart stores.
- Improved merchandising programs.
- Diversification projects complementing the strengths of the company's resources.

The company opened 71 K mart stores in 1983. Following the rapid store expansion program of the late 1970s when an average of 181 K mart stores opened per year, the company has shifted its emphasis to greater efficiency and productivity in existing stores during the 1980s. In 1983, projects to refurbish stores or add new departments totaled more than 2,100. In stores where these changes were made, significant sales increases were realized.

During the past three years, electronically based merchandise information systems have dramatically improved the efficiency of merchandising operations. The K mart Information Network ("KIN") connects K mart International Headquarters electronically to all U.S. K marts and is part of a series of systems that connect distribution centers, regional offices, subsidiaries and over 600 major vendors to K mart International Headquarters. Installation of KIN was completed in 1982. The conversion of men's and boys' wear to a centralized merchandising system administered by K mart Apparel Corp. was completed in late 1982. During its first complete year of operation in 1983, the operating results for this division were outstanding.

The company has refined its merchandise mix and presentation in response to the modern consumer's demand for better-quality items. Some examples of 1983 projects include:

- Home Electronic Centers were placed in 715 stores during the year. These departments sell home computers, peripheral equipment, software and entertainment game cartridges. K mart has become

a dominant retailer in home computers priced below \$500. Over 750 additional Home Electronic Centers will open during 1984.

- Kitchen Korner, introduced in 1982, offers brand-name fashion-oriented housewares. During 1983, 502 Kitchen Korner departments were completed, compared with 27 departments in the prior year. Kitchen Korners will be added to 650 K marts in 1984.
- Domestic Centers, which feature high-fashion soft goods for the home such as those found in traditional department stores, were introduced in 1983. A total of 91 departments were in place at the end of 1983, with plans to open 500 additional departments during 1984.
- Home Care Centers were in operation in 41 K mart stores at the end of 1983. Recognizing the importance of the growing do-it-yourself home improvement business, K mart will open up to 500 Home Care Centers over the next five years, 125 of which are planned for 1984.

During 1983, the company continued to expand, develop and seek compatible diversification opportunities outside of the general-merchandise retailing business.

Designer Depot is the company's entry into the highly competitive off-price specialty apparel field. A total of 28 Designer Depot stores were opened during 1983. K mart's expertise in merchandising apparel at discount prices provides an opportunity to capture a portion of this expanding market. The company plans to open an additional 30 Designer Depots during 1984.

Dining away from home is increasingly popular among Americans. To serve this trend, K mart has established a strong position in the cafeteria field through two subsidiaries. Furr's Cafeterias, Inc. ("Furr's") operates 117 cafeterias in the southwestern United States. Bishop Buffets, Inc. ("Bishop"), a chain of 30 cafeterias, was acquired by K mart on December 20, 1983. Based in Cedar Rapids, Iowa, Bishop operates in the midwestern and western United States. K mart issued 761,840 shares of common stock to complete the Bishop merger. The transaction has been accounted for as a pooling of interests. See Note (D) of the accompanying Notes to Consolidated Financial Statements for further information concerning Bishop.

The company intends to expand its activities in the financial services field through its wholly owned subsidiary, K mart Insurance Services, Inc. During 1983, 25 insurance centers were installed in K mart stores in Texas and Florida, bringing the total number of insurance centers operated by the company to 27. The insurance centers offer a full range of life, health and property/

casualty coverage. The company intends to open at least 50 additional insurance centers in Texas and Florida during 1984.

The company has committed resources to expand its merchandising export program. Through K mart Trading Services, Inc., a subsidiary primarily concerned with export activities of U.S.-made products, the company is enlarging its network of overseas agents and offices, thus creating marketing facilities for the distribution of merchandise throughout the world.

Several experimental retail units were introduced by the

company during 1983. K mart Canada Limited opened eight Big Top stores, which offer a limited assortment of basic merchandise at discount prices. In addition, K mart Corporation opened an experimental Accents store during 1983. Accents offers fine tableware and gifts at prices lower than normally found in department stores. The company plans to expand Big Top and Accents on a limited basis.

The company also opened a Garment Rack store in 1983. Garment Rack is a variation of Designer Depot which offers special buy opportunities for apparel not normally sold in Designer Depots.

| Five-Year Sales and Store Statistics                   | 1983     | 1982     | 1981     | 1980     | 1979     |
|--------------------------------------------------------|----------|----------|----------|----------|----------|
| <i>(Millions U.S. \$)</i>                              |          |          |          |          |          |
| Sales Analysis                                         |          |          |          |          |          |
| K mart                                                 | \$18,023 | \$16,192 | \$15,941 | \$13,655 | \$12,282 |
| Other                                                  | 575      | 580      | 586      | 549      | 449      |
| Total Sales                                            | \$18,598 | \$16,772 | \$16,527 | \$14,204 | \$12,731 |
| General Merchandise Stores                             |          |          |          |          |          |
| K mart Stores                                          |          |          |          |          |          |
| U.S.                                                   | 2,041    | 1,998    | 1,939    | 1,775    | 1,584    |
| Canada                                                 | 119      | 119      | 116      | 110      | 104      |
| Total K mart Stores                                    | 2,160    | 2,117    | 2,055    | 1,885    | 1,688    |
| Kresge and Jupiter Stores                              |          |          |          |          |          |
| U.S.                                                   | 143      | 187      | 252      | 287      | 310      |
| Canada                                                 | 58       | 66       | 67       | 70       | 71       |
| Total Kresge and Jupiter Stores                        | 201      | 253      | 319      | 357      | 381      |
| Total General Merchandise Stores                       | 2,361    | 2,370    | 2,374    | 2,242    | 2,069    |
| Cafeterias and Other Retail Units                      |          |          |          |          |          |
| Cafeterias                                             | 147      | 98       | 83       | 76       |          |
| Designer Depot                                         | 29       | 1        |          |          |          |
| Other Retail Units                                     | 10       | 2        |          |          |          |
| Canadian Shoe Retail                                   |          | 98       | 98       | 85       | 77       |
| Total Other Retail Units                               | 186      | 199      | 181      | 161      | 77       |
| <i>(Millions of square feet)</i>                       |          |          |          |          |          |
| Retail Selling Area                                    |          |          |          |          |          |
| K mart                                                 | 123.6    | 121.6    | 119.5    | 110.3    | 99.1     |
| Kresge, Jupiter, Designer Depot and Other Retail Units | 3.4      | 3.3      | 4.1      | 4.7      | 4.9      |
| Total Retail Selling Area                              | 127.0    | 124.9    | 123.6    | 115.0    | 104.0    |
| K mart Sales Per Square Foot*                          | \$ 155   | \$ 142   | \$ 146   | \$ 139   | \$ 138   |

\*Sales per square foot were calculated as follows: Total K mart sales plus unconsolidated sales of K mart licensees divided by total K mart store retail selling area for all K mart stores open for one full year as of the end of each fiscal year.

**Store Openings and Closings**—A total of 71 K marts were opened in 1983, consisting of 63 in the United States, five in Puerto Rico and three in Canada. During 1983, 28 Designer Depot stores and 20 Furr's cafeterias were opened. Of the K mart stores opened in 1983, seven were developed internally by K mart Corporation rather than by outside developers. Although the company has reduced its K mart store opening program, it remains committed to expansion in markets with high potential to improve market share. The company is represented in substantially all major metropolitan and several hundred rural markets in the contiguous United States. K mart also operates in Puerto Rico and in all provinces of Canada.

The company assesses profitability of individual stores on a continuing basis. Throughout 1983, the company continued to close selected stores that were operating at unacceptable levels of profitability. Twenty-eight K marts (including three in Canada), 52 Kresge and Jupiter stores (including eight Canadian locations), one cafeteria and eight other retail units were closed during 1983. Eight K marts, 66 Kresge and Jupiter stores and 361 automotive service departments were closed in 1982. Currently, K mart Corporation plans to close an additional eight K marts in 1984. The company's Canadian subsidiary, K mart Canada Limited, sold its unit that operated 92 free-standing shoe stores during 1983. The free-standing shoe stores had not met profit objectives established by management. Thus, the sale will allow more effective utilization of the company's resources.

K mart store selling area increased 1.6% in 1983 to 123.6 million square feet. Total retail selling area reached 127.0 million square feet in 1983, compared with 124.9 million and 123.6 million in 1982 and 1981, respectively.

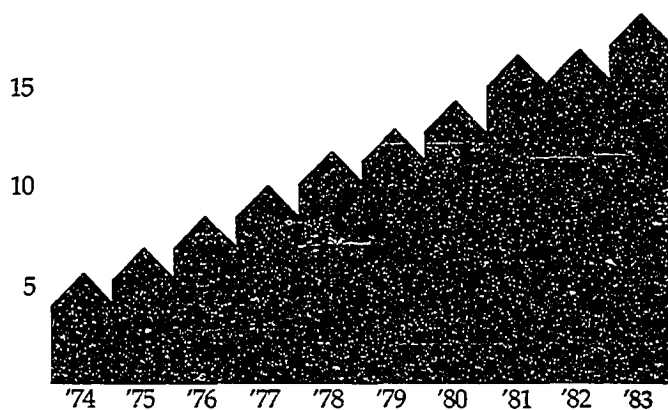
A summary of 1983 store openings and closings follows:

|                                   | K mart | Kresge &<br>Jupiter | Cafeterias | Other<br>Retail<br>Units | Total |
|-----------------------------------|--------|---------------------|------------|--------------------------|-------|
| Retail units in operation 1/26/83 | 2,117  | 253                 | 98         | 101                      | 2,569 |
| Units opened                      | 71     |                     | 20         | 38                       | 129   |
| Acquisitions                      |        |                     | 30         |                          | 30    |
| Units sold                        |        |                     |            | (92)                     | (92)  |
| Units closed                      | (28)   | (52)                | (1)        | (8)                      | (89)  |
| Retail units in operation 1/25/84 | 2,160  | 201                 | 147        | 39                       | 2,547 |

## SALES

(Billions)

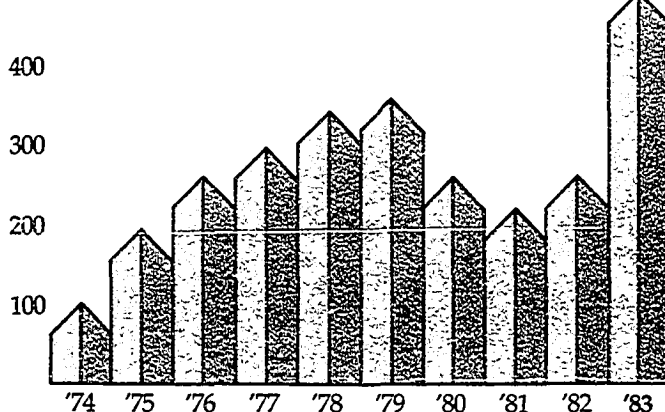
\$20



## NET INCOME

(Millions)

\$500



# MANAGEMENT'S DISCUSSION AND ANALYSIS OF OPERATIONS AND FINANCIAL CONDITION

## Results of Operations

**Sales**—In the improved economic environment of 1983, K mart Corporation's sales reached another record level. Consolidated sales were \$18.6 billion, an increase of 10.9% over 1982.

A three-year summary of the company's domestic and Canadian sales follows:

| (Millions U.S. \$) | 1983              | %<br>Increase | 1982              | %<br>Increase<br>(Decrease) | 1981              |
|--------------------|-------------------|---------------|-------------------|-----------------------------|-------------------|
| Domestic           | \$17,785.7        | 11.1          | \$16,007.1        | 1.6                         | \$15,752.3        |
| Canadian           | 812.2             | 6.2           | 765.1             | (1.2)                       | 774.7             |
| Total              | <u>\$18,597.9</u> | 10.9          | <u>\$16,772.2</u> | 1.5                         | <u>\$16,527.0</u> |

The 1983 sales increase was primarily due to increased consumer confidence, higher levels of employment, inflation and significant changes in the company's merchandising programs. The 1983 sales increase slightly exceeded management's expectations. Sales in comparable stores increased 9.2%. Sales from K mart stores accounted for 96.9% of total company business in 1983.

Consolidated sales in 1982 increased 1.5% over 1981 to \$16.8 billion. This level of increase was below company expectations. The modest 1982 sales gain resulted from the company's decision to de-emphasize 1981 promotional programs. Also a factor was consumer caution and concern caused by a weakened economy and continued high unemployment. Sales in comparable stores for the year decreased 1.4%.

**Income**—Income before estimated income taxes in 1983 was \$853.7 million, an increase of 103.8% from 1982. After a \$44.5 million pretax charge for store closings, income before estimated income taxes in 1982 was \$418.9 million, an increase of 29.7% from 1981.

The effective income tax rate for 1983 was 42.9%, compared with 38.7% in 1982 and 33.2% in 1981. The increase in 1983 was the result of higher earnings from operations relative to earnings from the company's equity interests, which are taxed at lower rates. This increase was partially offset by a tax credit for a Payroll-Based Stock Ownership Plan ("PAYSOP") adopted during the year. The increase in the effective income tax rate for 1982 resulted primarily from a decrease in investment tax credits due to fewer store openings than in 1981 and from increased earnings from operations in 1982. Additional information is summarized in Note (H) of the accompanying Notes to Consolidated Financial Statements.

Net income in 1983 was \$492.3 million, an increase of 88.0% over 1982. After a \$24.0 million net of tax charge for store closings, net income in 1982 was \$261.8 million, an increase of 18.9% over 1981.

A schedule of domestic and foreign net income follows:

| (Millions U.S. \$) | 1983           | %<br>Increase<br>(Decrease) | 1982           | %<br>Increase | 1981           |
|--------------------|----------------|-----------------------------|----------------|---------------|----------------|
| Domestic           | \$464.8        | 98.6                        | \$234.1        | 19.7          | \$195.6        |
| Foreign            | 27.5           | (.8)                        | 27.7           | 12.6          | 24.7           |
| Total              | <u>\$492.3</u> | 88.0                        | <u>\$261.8</u> | 18.9          | <u>\$220.3</u> |

Major factors contributing to net income results were:

**Cost of Merchandise Sold**—Cost of merchandise sold (including buying and occupancy costs) in 1983 was 72.3% of sales, compared with 73.3% in 1982 and 74.8% in 1981. Gross profit margins improved in 1983 to 27.7% of sales, compared with 26.7% in 1982 and 25.2% in 1981. The improved gross profit margins attained in 1983 and 1982 were the results of improved general economic conditions and planned changes in merchandise mix and presentation. These changes included the introduction of new product lines and selective expansion of brand-name merchandise assortments. During both years, the company emphasized sales of higher-margin items rather than strong promotion of low-margin items, while maintaining a strong competitive program.

The company reports inventory on the last-in, first-out ("LIFO") method of inventory valuation for substantially all domestic inventories to provide a more accurate matching of current costs with current revenues and to measure the impact of inflation on inventories during periods of rising prices. Based on the U.S. Department of Labor's Department Store Inventory Price Index for the year ended January 25, 1984, the inflationary impact on inventories was \$45.6 million in 1983, compared with \$25.7 million in 1982 and \$139.4 million in 1981.

**Operating Expenses**—Selling, general and administrative ("SGA") expenses, including advertising, were 23.1% of sales in 1983, compared with 23.9% for 1982 and 23.1% for 1981. The planned decrease in the 1983 SGA expense ratio was due to a favorable sales level and productivity gains. Although the SGA expense ratio for 1982 exceeded that of prior years due to lower than expected sales, the company had taken steps to improve productivity over the past several years, including implementation of electronic store systems and cost-reduction programs.

The following contributed to the increase in operating expenses in 1983 and 1982:

Employee compensation and benefits increased 3.9% to \$2.9 billion in 1983 and 6.3% to \$2.8 billion in 1982. This rate of increase was lower than in prior years due to fewer store openings, systems automation and merchandise ordering improvements. The Employees' Savings Plan, which became effective in July 1982, contributed to the increases in 1983 and 1982. The plan provides for the company to match half of employee contributions up to 6% of eligible compensation. Total pension expense was \$42.2 million in 1983 and \$42.7 million in 1982. The decrease in 1983 was due to a change in the assumed rate of employee turnover based on the company's actual experience, partially offset by a general increase in pension costs.

Payroll, property and franchise taxes increased 8.2% to \$356.8 million in 1983 and 7.8% to \$329.8 million in 1982. These increases were primarily due to increased payroll taxes, property taxes and other taxes on existing stores.

Depreciation and amortization expense for owned property increased 6.6% to \$167.8 million in 1983 and 11.9% to \$157.4 million in 1982. The increases resulted from new store openings and extensive refurbishing programs in existing stores.

*Net Interest Expense on Debt*—Net interest expense related to debt in 1983 was \$46.1 million, an increase of 7.0% from 1982. The increase in 1983 net interest expense resulted primarily from lower interest yields on funds invested compared with the prior year. Net interest expense related to debt in 1982 was \$43.1 million, a decrease of 37.8% from 1981. The decrease in 1982 was the result of declining interest rates, the reduced K mart store opening program and lower borrowing levels net of temporary investments. The weighted average interest rates for short-term borrowings were 9.6%, 11.7% and 15.7% for 1983, 1982 and 1981, respectively.

*Foreign Operations*—K mart Canada Limited's sales for 1983 (in Canadian dollars) increased 6.1% from 1982, compared with a 1.7% increase in 1982 over 1981. Sales, excluding

free-standing shoe stores, increased 7.3% in 1983 compared with 1982. Income from operations in 1983 increased over 1982 primarily due to better than anticipated sales in the K mart division and good expense control. Net income in 1983 also included a \$3.9 million (in Canadian dollars) gain on the sale of real estate.

After careful consideration, K mart Canada Limited decided to redeploy some of its assets into channels with greater potential for future growth. Accordingly, certain operations that did not meet profit objectives were discontinued or sold. Canmart Shoe Ltd., which operated 92 free-standing shoe stores, was sold to a privately owned company. The sale did not affect shoe departments in Canadian K mart stores. Also, three Canadian K marts were closed in 1983, with plans to close an additional three in 1984.

The company's income (before currency gains) from Australian operations, which consisted primarily of equity income in G. J. Coles & Coy. Limited ("Coles"), was \$18.1 million in 1983, compared with \$16.2 million in 1982 and \$17.4 million in 1981. The application of Financial Accounting Standards No. 52, "Foreign Currency Translation," resulted in no currency fluctuation in 1983, compared with a gain of \$7.0 million in 1982 and \$2.7 million in 1981. Equity income (before currency gains) from Australian operations was adversely affected in 1983 and 1982 by a declining average exchange rate of the Australian dollar to the U.S. dollar. The average exchange rate was .9067, 1.0221 and 1.1522 in 1983, 1982 and 1981, respectively. Coles' sales reached \$4.7 billion in Australian dollars at July 31, 1983 (Coles' latest fiscal year-end), compared with \$4.0 billion for fiscal 1982, an increase of 17.2%. Sales in Australian dollars for fiscal 1982 increased 24.7% over fiscal 1981 sales of \$3.2 billion. Pretax profit from operations in Australian dollars rose 20.6% to \$155.7 million in 1983 and 9.9% to \$129.1 million in 1982, compared with respective prior years. During fiscal 1983, Coles opened 52 stores, including 13 K marts, bringing the total number of stores operated by Coles in Australia to 885, including 86 K marts. Among the K marts opened in 1983 were four

new Super K mart stores, which combine food and general-merchandise operations. For additional information on the company's investment in Coles, see Note (F) of the accompanying Notes to Consolidated Financial Statements.

The company holds a 44% interest in Astra, S.A. ("Astra"), a retailing subsidiary of the Gentor Group of Monterrey, Mexico. The food and general-merchandise subsidiaries operate seven Astra discount-type stores and ten self-service food-type Autodescuento stores. The company's equity share of Astra's results for their year ended December 31, 1983 was a \$5.7 million loss, compared with a \$9.0 million loss in 1982. The weak Mexican economy, increased competition and interest expense on debt related to the planned store expansion program have prevented Astra from achieving profitability in 1983 and 1982. The effect on the company's equity resulting from three major devaluations in Mexico during 1982 was not significant. For further information regarding the company's investment in Astra, see Notes (D) and (K) of the accompanying Notes to Consolidated Financial Statements.

*Licensee Operations*—The company's U.S. K mart footwear departments are operated by the Meldisco subsidiaries of Melville Corporation. Sales of the licensee footwear departments increased 11.7% to \$848.4 million in 1983 and 10.3% to \$759.3 million in 1982, compared with respective prior years. Equity in income rose 26.1% to \$40.2 million in 1983 and 15.0% to \$31.9 million in 1982, compared with respective prior years. The increase in income for 1983 was attributable to increased sales and improved gross margins resulting from merchandise sales mix improvements. Refer to Note (F) of the accompanying Notes to Consolidated Financial Statements for further information regarding the company's investment in Meldisco.

Additionally, the company receives fee income under a license agreement established in 1980 with The Daiei, Inc. ("Daiei"), the largest retailer in Japan. K mart provides Daiei with knowledge and assistance to develop mass merchandising operations in Japan and the exclusive right to use various K mart tradenames and trademarks.

*Furr's Cafeterias, Inc.*—Furr's Cafeterias, Inc. ("Furr's"), a wholly owned subsidiary of K mart, operates a chain of cafeterias in the southwestern U.S. As of January 25, 1984, there were 117 cafeterias in operation. Furr's sales increased 17.3% in 1983, compared with increases of 20.0% in 1982 and 18.5% in 1981.

*Bishop Buffets, Inc.*—Bishop Buffets, Inc. ("Bishop") was acquired by the company on December 20, 1983. K mart issued 761,840 shares of common stock to complete the transaction. The acquisition has been accounted for as a pooling of interests; however, the financial statements have not been restated for periods prior to the acquisition due to immateriality. Bishop operates a chain of cafeterias in the midwestern and western United States. At January 25, 1984, 30 cafeterias were in operation. Bishop's sales increased 9.7% in 1983, compared with an increase of 7.3% in 1982. See Note (D) of the accompanying Notes to Consolidated Financial Statements for further information concerning Bishop.

*Insurance Operations*—K mart Insurance Services, Inc. ("KMI"), a wholly owned insurance subsidiary, has continued to expand into new marketing areas. In addition to supporting various insurance systems of K mart Corporation, KMI now markets life, health and property/casualty insurance through selected K mart stores. Insurance centers operated in 27 K mart stores in 1983, with at least 50 planned to open in 1984. KMI's insurance premiums and other revenues for 1983 were \$112.9 million, compared with \$95.7 million in 1982, an increase of 18.0%. Net income in 1983 was \$5.1 million, compared with \$4.9 million in 1982, an increase of 4.1%. See Note (F) of the accompanying Notes to Consolidated Financial Statements for additional information on KMI.

*Inflation Accounting*—A discussion of the impact of inflation on the company's sales and earnings is presented on pages 24 and 25.

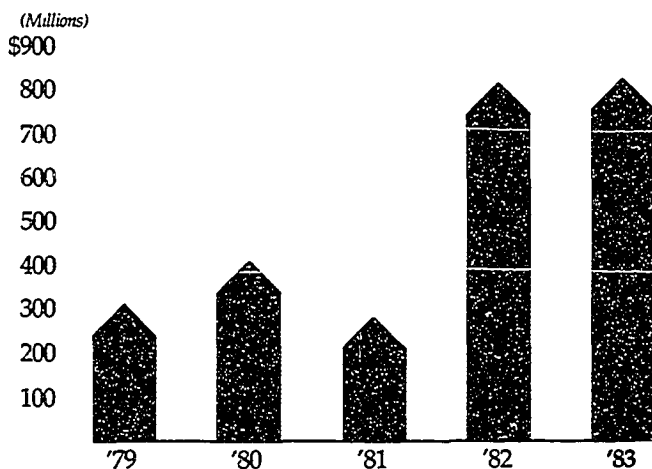
## Financial Condition

K mart Corporation's financial policy is designed to provide a solid capital structure utilizing its available sources of funds. The company has maintained a strong position of liquidity over the years as well as a high degree of financial flexibility, based primarily on a large flow of funds from operations. The company's debt structure (even when capital leases are included) and its strong financial position enable K mart Corporation to obtain necessary funds at the best available rates in worldwide capital markets.

K mart employs a number of criteria to carefully monitor adherence to the company's financial policy. Among these criteria are trends in cash flow, working capital, financial ratio analysis and the capitalization structure of the company.

**Cash Flow**—Net cash provided by operations is a demonstration of the company's performance and enables the company to internally fund growth in new store openings, refurbishing programs, acquisitions, systems development, dividends to shareholders and debt repayment.

### NET CASH PROVIDED BY OPERATIONS



A summary of the company's changes in cash position follows:

| (Millions)                      | 1983    | 1982    | 1981     |
|---------------------------------|---------|---------|----------|
| Net cash provided by operations | \$819.8 | \$807.5 | \$278.1  |
| Net cash provided by financing  | 139.3   | 102.8   | 314.0    |
| Dividends paid                  | (132.2) | (123.0) | (117.5)  |
| Net cash used for investments   | (353.0) | (348.7) | (572.4)  |
| Net increase (decrease) in cash | \$473.9 | \$438.6 | \$(97.8) |

Refer to the company's Consolidated Statements of Changes in Financial Position on page 30 for additional information.

Net cash provided by operations, which was \$819.8 million in 1983, \$807.5 million in 1982 and \$278.1 million in 1981, produced a major source of cash needed to operate the business. Net cash provided by operations is primarily a function of earnings, which increased substantially in 1983 compared with the prior year. Depreciation and amortization expense, also a major component of net cash provided by operations, has been steadily increasing each year due to the continued high level of capital expenditures. The increase in net cash provided by operations in 1982 was attributable to increased earnings, reduction of inventory investment due to changes in merchandise mix and the timing of income tax liabilities.

Net cash provided by financing was \$139.3 million in 1983, \$102.8 million in 1982 and \$314.0 million in 1981. The increase in 1983 was primarily attributable to an increase in long-term debt and notes payable. During 1983, additional debt obligations consisting of \$120.7 million of commercial paper supported by long-term credit agreements with several banks were classified as long-term debt. The reduction in 1982 of net cash provided by financing occurred primarily because there were no significant additions to long-term debt and notes payable compared with 1981. However, during 1982, debt obligations consisting of \$179.3 million of commercial paper supported by long-term credit agreements with several banks were classified as long-term debt. See Note (I) in the accompanying Notes to Consolidated Financial Statements for more information.

Because of the seasonal nature of the retail industry, K mart utilizes commercial paper and revolving bank credit to cover peak working capital requirements. The maximum amounts of aggregate short-term borrowings outstanding during 1983, 1982 and 1981 were \$459.1 million, \$894.3 million and \$999.6 million, respectively. The approximate average short-term borrowings outstanding during 1983, 1982 and 1981 were \$250.8 million, \$524.8 million and \$520.5 million, respectively.

Total short-term lines of credit available and unused were \$803.6 million, \$685.3 million and \$852.6 million at January 25, 1984, January 26, 1983 and January 27, 1982, respectively.

The company expects that funds required to finance future expansion will be provided primarily from internally generated funds and leasing of land and buildings. In addition, the company may issue common stock from time to time for acquisitions and to support stock option and employees' savings plans. The company will continue to utilize short-term borrowings, primarily commercial paper, to cover peak working capital requirements.

Net cash used for investments increased to \$353.0 million in 1983, compared with \$348.7 million in 1982. Major factors contributing to the 1983 increase were the company's K mart and Designer Depot store opening programs, a continuation of the store modernization program and expansion of merchandising systems. As a result of the company's reduced K mart store opening program, net cash used for investments has decreased over the past two years relative to the average of \$556.3 million per year between 1979 and 1981. These reductions were in accord with the company's strategy of devoting more financial resources to existing facilities and other retail units rather than rapid expansion of new K mart stores.

**Working Capital**—Working capital management is indicative of the company's financial flexibility to meet ongoing business obligations.

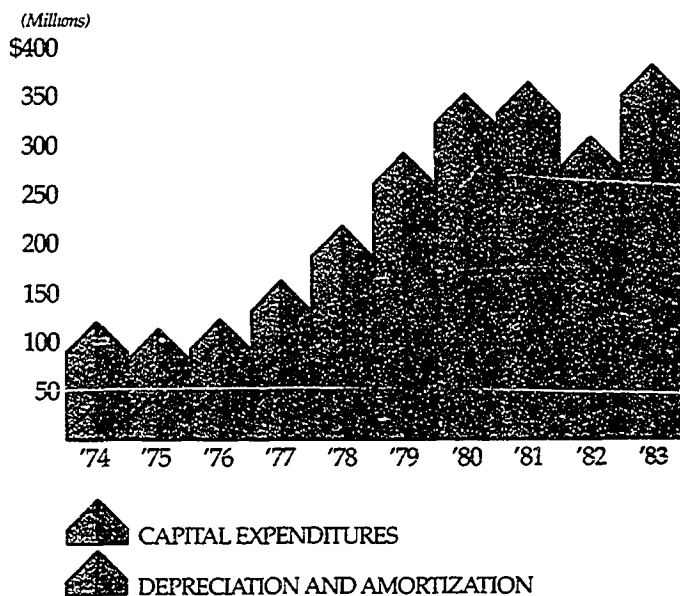
An analysis of the changes in working capital follows:

| (Millions)                                                              | 1983             | 1982             | 1981             |
|-------------------------------------------------------------------------|------------------|------------------|------------------|
| Increase (decrease) in current assets:                                  |                  |                  |                  |
| Cash and temporary investments                                          | \$ 473.9         | \$ 438.6         | \$ (97.8)        |
| Accounts receivable                                                     | 19.0             | 25.9             | 10.1             |
| Merchandise inventories                                                 | 286.7            | 159.8            | 289.2            |
| Operating supplies and prepaid expenses                                 | 5.3              | (18.5)           | 12.7             |
|                                                                         | <b>784.9</b>     | <b>605.8</b>     | <b>214.2</b>     |
| Increase (decrease) in current liabilities:                             |                  |                  |                  |
| Obligations under capital leases and long-term debt due within one year | 3.0              | 6.7              | 5.1              |
| Notes payable                                                           |                  | (168.2)          | 168.2            |
| Accounts payable – trade                                                | 203.8            | 260.4            | 192.8            |
| Accrued payrolls, taxes and other liabilities                           | 40.8             | 69.0             | (7.1)            |
| Dividends payable                                                       | 2.9              | 1.4              | 1.4              |
| Income taxes                                                            | 93.9             | 82.1             | (67.2)           |
|                                                                         | <b>344.4</b>     | <b>251.4</b>     | <b>293.2</b>     |
| Increase (decrease) in working capital                                  | \$ 440.5         | \$ 354.4         | \$ (79.0)        |
| Total working capital                                                   | <b>\$2,267.7</b> | <b>\$1,827.2</b> | <b>\$1,472.8</b> |

Working capital increased \$440.5 million in 1983, compared with a \$354.4 million increase in 1982. The increase is largely attributable to substantially improved operating results. The classification of commercial paper as long-term debt of \$179.3 million in 1982 and an additional \$120.7 million in 1983 was also a major factor contributing to the increases in working capital in both 1983 and 1982.

The decrease in working capital in 1981 was partially due to the acquisition of 44% of Astra, S.A., previously a wholly owned retail subsidiary of the Gentor Group of Monterrey, Mexico, for \$50.0 million in cash.

## CAPITAL EXPENDITURES AND DEPRECIATION AND AMORTIZATION—OWNED ASSETS



**Financial Ratios**—Efficiency in inventory management is indicated by K mart's first-in, first-out ("FIFO") inventory turnover ratio using replacement cost as measured by the FIFO method of inventory valuation. The inventory turnover ratio was 3.3 in 1983, compared with 3.2 in 1982 and 3.5 in 1981.

The current ratio is indicative of the company's ability to meet short-term obligations. K mart's current ratio was 1.9 in 1983, compared with 1.8 in both 1982 and 1981. The 1983 improvement was a result of substantially improved results of operations and the inclusion of \$300.0 million of notes payable in long-term debt at January 25, 1984, compared with \$179.3 million at January 26, 1983, under revolving credit agreements with various banks.

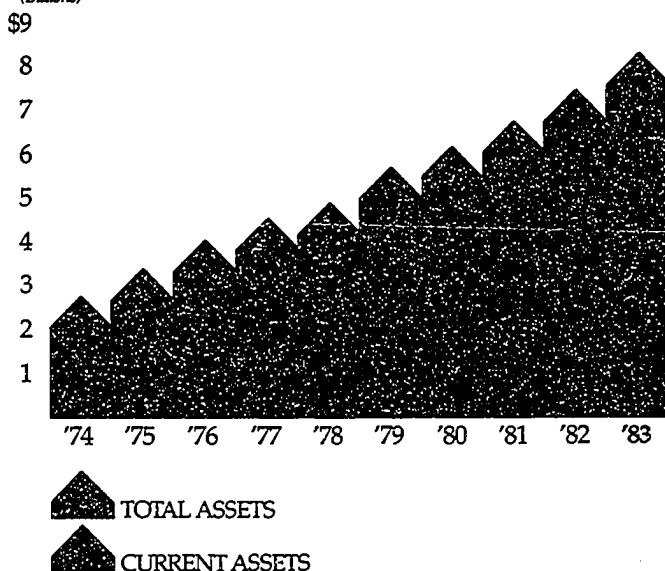
The ratio of income to fixed charges, which was 3.4, 2.2 and 1.9 in 1983, 1982 and 1981, respectively, demonstrates the company's ability to cover charges of a fixed nature, consisting primarily of interest expense, in relation to net income. Increasing net income and declining interest rates were the primary factors in the improvement in the ratio of income to fixed charges in 1983 and 1982.

**Capitalization Structure**—The long-term liquidity of K mart is indicated by the debt-to-total-capitalization ratio, which was 47.0%, 48.7% and 47.2% in 1983, 1982 and 1981, respectively.

| (Millions)                                           | 1983      | %     | 1982      | %     | 1981      | %     |
|------------------------------------------------------|-----------|-------|-----------|-------|-----------|-------|
| Long-term debt due within one year                   | \$ 3.2    |       | \$ 5.1    | .1    | \$ 1.8    |       |
| Obligations under capital leases due within one year | 70.6      | 1.2   | 65.7      | 1.3   | 62.3      | 1.3   |
| Long-Term Debt                                       | 711.2     | 12.6  | 596.0     | 11.5  | 415.1     | 8.8   |
| Obligations under Capital Leases                     | 1,822.3   | 32.2  | 1,824.4   | 35.3  | 1,752.0   | 36.9  |
| Other                                                | 56.6      | 1.0   | 26.8      | .5    | 10.2      | .2    |
| Total debt and equivalent                            | 2,663.9   | 47.0  | 2,518.0   | 48.7  | 2,241.4   | 47.2  |
| Deferred Income Taxes                                | 60.9      | 1.1   | 51.6      | 1.0   | 51.4      | 1.1   |
| Equity                                               | 2,940.1   | 51.9  | 2,601.3   | 50.3  | 2,455.6   | 51.7  |
| Total capitalization                                 | \$5,664.9 | 100.0 | \$5,170.9 | 100.0 | \$4,748.4 | 100.0 |

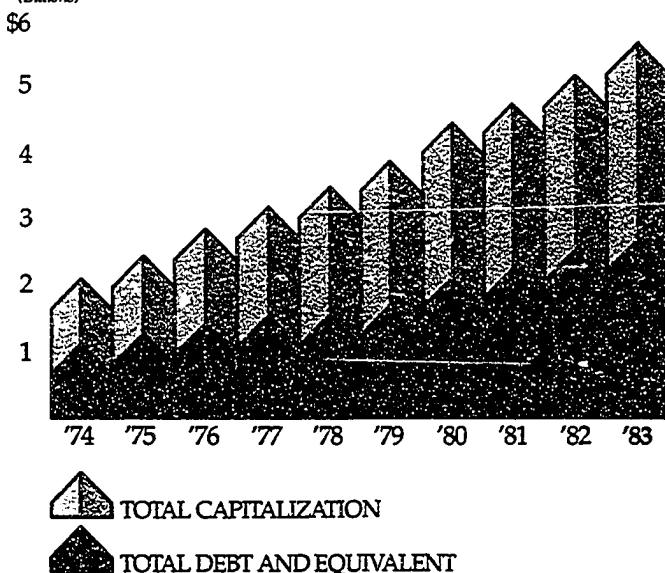
## TOTAL AND CURRENT ASSETS

(Billions)



## CAPITALIZATION

(Billions)



## Shareholders' Information

**Shareholders' Equity**—Shareholders' equity reached \$2.9 billion in 1983, compared with \$2.6 billion in 1982, an increase of 13.0%. Book value per share was \$23.35 for 1983, compared with \$20.89 for 1982. Over the past ten years, the compound growth rate for book value per share was 12.0%. Return on beginning shareholders' equity was 18.9% for 1983, the highest level achieved since 1978.

Dividends of \$132.2 million were paid to K mart shareholders during 1983, compared with \$123.0 million in 1982, an increase of 7.5%. K mart increased dividends declared to shareholders in 1983 for the 19th consecutive year. Dividends declared were \$1.08 per share, an increase of 8.0% over the annual rate of \$1.00 per share in 1982. Over the past ten years, the compound growth rate for dividends declared per share was 18.4%.

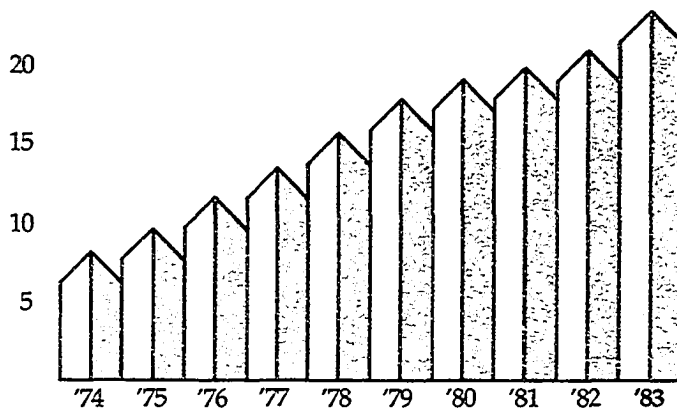
On January 25, 1984, there were 94,721 holders of K mart's common stock, which is listed and traded on the New York and Pacific Stock Exchanges (trading symbol KM). A summary of the dividends paid per common share and the high and low market prices of K mart common stock during the past two years follows:

| Quarter | Fiscal Quarter    |                   | Calendar Quarter                      |                                       |
|---------|-------------------|-------------------|---------------------------------------|---------------------------------------|
|         | 1983<br>Dividends | 1982<br>Dividends | 1983 Market<br>Prices<br>(High - Low) | 1982 Market<br>Prices<br>(High - Low) |
| First   | \$ .25            | \$ .24            | 34 - 21¾                              | 18½ - 15½                             |
| Second  | .27               | .25               | 36¾ - 30½                             | 19½ - 17½                             |
| Third   | .27               | .25               | 38½ - 30¾                             | 22½ - 15½                             |
| Fourth  | .27               | .25               | 39¾ - 32½                             | 27¼ - 20½                             |
| Year    | <u>\$1.06</u>     | <u>\$ .99</u>     | 39¾ - 21¾                             | 27¼ - 15½                             |

## SHAREHOLDERS' BOOK VALUE PER SHARE

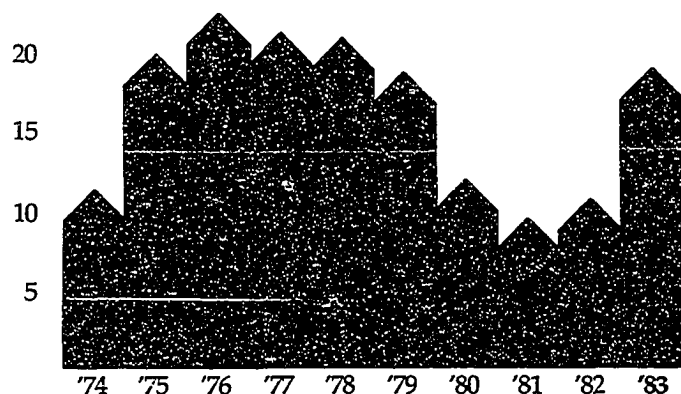
(Dollars)

\$25



## RETURN ON SHAREHOLDERS' EQUITY (BEGINNING)

25%



## *Impact of Inflation (Unaudited)*

*Introduction*—Under generally accepted accounting principles, financial statements traditionally have been prepared on the basis of historical cost. However, continued high rates of inflation over the past decade have eroded the purchasing power of the dollar and distorted financial information prepared on a historical cost basis. In an attempt to demonstrate the impact of inflation, the Financial Accounting Standards Board issued Statement No. 33 ("FAS 33"), "Financial Reporting and Changing Prices." Under FAS 33, as amended by FAS 70, disclosure requirements provide for presentation of inflation under the current cost method which reflects the company's specific inflation experience.

The current cost method attempts to provide reasonable approximations of changes in specific prices of goods and services applicable to individual corporations from the dates they were acquired to the present.

Under the guidelines of FAS 33, only cost of merchandise sold and depreciation and amortization expenses are required to be adjusted, since these components of the income statement are thought to be most affected by inflation.

*Discussion of Results*—The company's net income, as reported in the audited financial statements on a historical basis, is determined by use of the LIFO method of inventory valuation to compute cost of merchandise sold for 88.5% of inventories at January 25, 1984. Most nonfood retailers, including K mart, employ the LIFO method and use the Bureau of Labor Statistics Index ("BLS") to measure inflation in cost of merchandise sold. For purposes of inflation-adjusted financial statements, non-LIFO inventories are converted to an estimated LIFO value using the BLS index. Thus, cost of merchandise sold approximates current costs.

Depreciation and amortization expense for owned and leased properties in 1983 was \$404.8 million on a current cost basis. Current cost depreciation is calculated using a combination of average costs and building indexes for owned and leased assets.

Inflation accounting calculations were also made for leased property. Under FAS 33, capitalization of leased property is inflation-affected but operating leases are not. Amortization expense is not comparable among other retail companies, as the application of Statement of Financial Accounting Standards No. 13, "Accounting for Leases," is not uniformly applied within the retail industry.

One of the most significant effects of inflation is the application of income taxes. In accordance with FAS 33, income tax expense remains the same for current cost accounting as that reported in the historical financial statements. Present tax laws do not allow deductions for additional cost of merchandise sold and depreciation expense resulting from the effects of inflation. As a result, the effective tax rate for 1983 rises from 42.9% on a historical cost basis to 51.7% on a current cost basis.

A "purchasing power gain" is created where monetary liabilities (such as capital lease obligations and long-term debt) exceed monetary assets (cash, receivables, etc.). This net monetary liability position results in a gain in purchasing power since the obligation will presumably be settled in dollars of lower value. Such a gain does not represent earnings nor funds available for dividends. A major factor in the company's gain in purchasing power results from the substantial use of capital lease financing that approximates 46.5% of the net amounts owed.

The current cost method involves the use of assumptions, approximations and estimates. Thus, this method should be viewed in this context and not as a precise indicator of the effects of inflation on K mart Corporation.

# Statements of Income Adjusted for Changing Prices

Fiscal Year Ended January 25, 1984

| <i>(Millions)</i>                                                                                   | As Reported in<br>the Primary<br>Financial<br>Statements | Adjusted for<br>Changes in<br>Specific Prices<br>(Current Cost) |
|-----------------------------------------------------------------------------------------------------|----------------------------------------------------------|-----------------------------------------------------------------|
| Sales and other income                                                                              | \$18,841.0                                               | \$18,841.0                                                      |
| Cost of merchandise sold                                                                            | 13,321.3                                                 | 13,326.2                                                        |
| Depreciation and amortization                                                                       | 264.4                                                    | 404.8                                                           |
| Other costs and expenses                                                                            | 4,401.6                                                  | 4,401.6                                                         |
| Income before estimated income taxes                                                                | 853.7                                                    | 708.4                                                           |
| Estimated income taxes                                                                              | 366.5                                                    | 366.5                                                           |
| Net income (includes \$5.1 equity in<br>income of insurance operations)                             | \$ 492.3                                                 | \$ 347.0                                                        |
| Effective tax rate                                                                                  | 42.9%                                                    | 51.7%                                                           |
| Unrealized gain from decline in purchasing power of net<br>amounts owed                             |                                                          | \$ 164.9                                                        |
| Increase in specific prices (current cost) of merchandise inventories,<br>property owned and leased |                                                          | \$ 487.3                                                        |
| Increase in general price level (constant dollar)                                                   |                                                          | 356.6                                                           |
| Excess of increase in specific prices over increase in general price level                          |                                                          | \$ 130.7                                                        |

## Five-Year Comparison of Selected Supplementary Financial Data Adjusted for Effects of Changing Prices

*(Millions \$, except per share amounts, of average fiscal 1983 dollars)*

|                                                                                          | Fiscal Year Ended   |                     |                     |                     |                     |
|------------------------------------------------------------------------------------------|---------------------|---------------------|---------------------|---------------------|---------------------|
|                                                                                          | January 25,<br>1984 | January 26,<br>1983 | January 27,<br>1982 | January 28,<br>1981 | January 30,<br>1980 |
| Net sales and other operating revenue<br>(in constant dollars)                           | \$18,841.0          | \$17,536.7          | \$18,259.9          | \$17,283.7          | \$17,566.2          |
| Current cost:                                                                            |                     |                     |                     |                     |                     |
| Net income                                                                               | \$ 347.0            | \$ 140.5            | \$ 91.3             | \$ 198.7            | \$ 365.0            |
| Earnings per share                                                                       | \$ 2.69             | \$ 1.13             | \$ .76              | \$ 1.59             | \$ 2.90             |
| Net assets                                                                               | \$ 5,619.6          | \$ 5,049.0          | \$ 5,095.4          | \$ 4,684.9          | \$ 4,562.7          |
| Excess of increase (decrease) in specific<br>prices over increase in general price level | \$ 130.7            | \$ (52.9)           | \$ 219.7            | \$ (261.9)          | \$ (630.6)          |
| Gain from decline in purchasing power of<br>net amounts owed                             | \$ 164.9            | \$ 154.1            | \$ 327.4            | \$ 434.3            | \$ 505.2            |
| Other data (in constant dollars):                                                        |                     |                     |                     |                     |                     |
| Cash dividends declared per share                                                        | \$ 1.08             | \$ 1.03             | \$ 1.05             | \$ 1.11             | \$ 1.14             |
| Market price per share at year-end                                                       | \$ 31               | \$ 26               | \$ 17               | \$ 20               | \$ 28               |
| Average Consumer Price Index                                                             | 299.4               | 290.0               | 274.2               | 249.1               | 219.8               |

Constant dollar information is adjusted for general inflation as measured by the CPI-U, and current cost information is adjusted for changes in specific prices.

At January 25, 1984, current cost of merchandise inventories was \$4,108.2, current cost of property owned (net of accumulated depreciation) was \$1,732.4, and current cost of leased property under capital leases (net of accumulated amortization) was \$3,316.8.

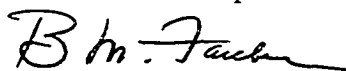
# REPORTS BY MANAGEMENT AND INDEPENDENT ACCOUNTANTS

## Kmart Responsibility for Financial Statements

Kmart Corporation management is responsible for the integrity of the information and representations contained in this annual report. This responsibility includes making informed estimates and judgments in selecting the appropriate accounting principles in the circumstances. Management believes the financial statements conform with generally accepted accounting principles and have been prepared on a consistent basis except for the change in the method of accounting for foreign currency translation, effective January 27, 1983, as described in Note (B) to the consolidated financial statements.

To assist management in fulfilling these obligations, the company utilizes several tools, which include the following:

- The company maintains a system of internal accounting controls to provide reasonable assurance that, among other things, financial records are reliable for purposes of preparing financial statements and the assets are properly accounted for and safeguarded. This concept of reasonable assurance is based on the recognition that the cost of the system must be related to the benefits to be derived. Management believes its system provides this appropriate balance.
- An Internal Audit Department is maintained to evaluate, test and report the application of internal accounting controls in conformity with the standards of the practice of internal auditing.
- The Board of Directors appoints the independent accountants to perform an examination of the company's financial statements. This examination includes, among other things, a review of the system of internal controls as required by generally accepted auditing standards.
- The Audit Committee of the Board of Directors, consisting solely of outside directors, meets regularly with management, internal auditors and independent accountants to assure that each is carrying out its responsibilities. The internal auditors and independent accountants both have full and free access to the Audit Committee, with and without the presence of management.



B. M. FAUBER  
Chairman of the Board  
and Chief Executive Officer



R. E. BREWER  
Executive Vice President  
Finance

## Report of Independent Accountants

To the Shareholders and Board of Directors of Kmart Corporation

In our opinion, the accompanying consolidated balance sheets and the related consolidated statements of income, of income retained for use in the business and of changes in financial position present fairly the financial position of Kmart Corporation and its subsidiaries at January 25, 1984 and January 26, 1983, and the results of their operations and the changes in their financial position for each of the three fiscal years in the period ended January 25, 1984, in conformity with generally accepted accounting principles consistently applied during the period except for the change effective January 27, 1983, with which we concur, in the method of accounting for foreign currency translation as described in Note (B) to the consolidated financial statements. Our examinations of these statements were made in accordance with generally accepted auditing standards and accordingly included such tests of the accounting records and such other auditing procedures as we considered necessary in the circumstances.

Detroit, Michigan  
March 7, 1984



# CONSOLIDATED STATEMENTS OF INCOME

| (Millions)                                                      | Fiscal Year Ended   |                     |                     |
|-----------------------------------------------------------------|---------------------|---------------------|---------------------|
|                                                                 | January 25,<br>1984 | January 26,<br>1983 | January 27,<br>1982 |
| Sales                                                           | \$18,597.9          | \$16,772.2          | \$16,527.0          |
| Licensee fees and rental income                                 | 191.3               | 169.5               | 151.6               |
| Equity in income of affiliated retail companies                 | 51.7                | 44.5                | 44.4                |
| Interest income                                                 | 38.0                | 54.6                | 45.7                |
|                                                                 | 18,878.9            | 17,040.8            | 16,768.7            |
| Cost of merchandise sold (including buying and occupancy costs) | 13,447.4            | 12,298.6            | 12,360.4            |
| Advertising                                                     | 424.6               | 401.7               | 385.7               |
| Selling, general and administrative expenses                    | 3,880.1             | 3,602.9             | 3,424.0             |
| Provision for store closings                                    |                     | 44.5                |                     |
| Interest expense:                                               |                     |                     |                     |
| Debt                                                            | 84.1                | 97.7                | 114.9               |
| Capital lease obligations                                       | 189.0               | 176.5               | 160.8               |
|                                                                 | 18,025.2            | 16,621.9            | 16,445.8            |
| Income before estimated income taxes                            | 853.7               | 418.9               | 322.9               |
| Estimated income taxes:                                         |                     |                     |                     |
| U.S.                                                            | 304.7               | 131.7               | 73.9                |
| Foreign                                                         | 4.8                 | 3.1                 | 4.4                 |
| State and local                                                 | 35.5                | 19.6                | 17.1                |
| Tax effects of timing differences                               | 21.5                | 7.6                 | 11.8                |
|                                                                 | 366.5               | 162.0               | 107.2               |
| Income from retail operations                                   | 487.2               | 256.9               | 215.7               |
| Equity in income of insurance operations                        | 5.1                 | 4.9                 | 4.6                 |
| Net income for the year                                         | \$ 492.3            | \$ 261.8            | \$ 220.3            |
| Earnings per common and common equivalent share                 | \$3.80              | \$2.06              | \$1.75              |

## CONSOLIDATED STATEMENTS OF INCOME RETAINED FOR USE IN THE BUSINESS

| (Millions)                                                                                      | Fiscal Year Ended   |                     |                     |
|-------------------------------------------------------------------------------------------------|---------------------|---------------------|---------------------|
|                                                                                                 | January 25,<br>1984 | January 26,<br>1983 | January 27,<br>1982 |
| Income retained for use in the business at beginning of year                                    | \$ 2,204.9          | \$ 2,067.4          | \$ 1,966.0          |
| Net income for the year                                                                         | 492.3               | 261.8               | 220.3               |
| Cash dividends declared—\$1.08, \$1.00 and \$.96, respectively                                  | (135.1)             | (124.3)             | (118.9)             |
| Cumulative retained earnings of Bishop Buffets, Inc., at the date of acquisition [See Note (D)] | 7.0                 |                     |                     |
| Income retained for use in the business at end of year                                          | \$ 2,569.1          | \$ 2,204.9          | \$ 2,067.4          |

See Notes to Consolidated Financial Statements.

# CONSOLIDATED BALANCE SHEETS

| (Millions)                                                                                                  | January 25,<br>1984 | January 26,<br>1983 |
|-------------------------------------------------------------------------------------------------------------|---------------------|---------------------|
| <b>Assets</b>                                                                                               |                     |                     |
| Current Assets:                                                                                             |                     |                     |
| Cash (includes temporary investments of \$762.9<br>and \$449.4, respectively)                               | \$1,027.7           | \$ 553.8            |
| Accounts receivable                                                                                         | 134.8               | 115.8               |
| Merchandise inventories                                                                                     | 3,581.6             | 3,294.9             |
| Operating supplies and prepaid expenses                                                                     | 44.4                | 39.1                |
| Total current assets                                                                                        | 4,788.5             | 4,003.6             |
| Investments in and Advances to:                                                                             |                     |                     |
| Affiliated retail companies                                                                                 | 211.8               | 216.4               |
| Insurance operations                                                                                        | 128.6               | 114.3               |
| Other Assets and Deferred Charges                                                                           | 80.5                | 72.5                |
| Property:                                                                                                   |                     |                     |
| Land                                                                                                        | 57.6                | 56.6                |
| Buildings                                                                                                   | 174.4               | 179.5               |
| Leasehold improvements                                                                                      | 303.9               | 276.4               |
| Furniture and fixtures                                                                                      | 1,738.0             | 1,589.1             |
| Construction in progress                                                                                    | 57.5                | 41.6                |
|                                                                                                             | 2,331.4             | 2,143.2             |
| Less—Depreciation and amortization                                                                          | 976.6               | 858.0               |
| Total property owned                                                                                        | 1,354.8             | 1,285.2             |
| Leased property under capital leases, less accumulated<br>amortization of \$767.2 and \$701.1, respectively | 1,618.9             | 1,651.7             |
| Total property                                                                                              | 2,973.7             | 2,936.9             |
|                                                                                                             | \$8,183.1           | \$7,343.7           |

See Notes to Consolidated Financial Statements.

| <b>Liabilities and Shareholders' Equity</b>          | <b>January 25,<br/>1984</b> | <b>January 26,<br/>1983</b> |
|------------------------------------------------------|-----------------------------|-----------------------------|
| <b>Current Liabilities:</b>                          |                             |                             |
| Long-term debt due within one year                   | \$ 3.2                      | \$ 5.1                      |
| Obligations under capital leases due within one year | 70.6                        | 65.7                        |
| Accounts payable—trade                               | 1,717.2                     | 1,513.4                     |
| Accrued payrolls and other liabilities               | 294.0                       | 263.0                       |
| Taxes other than income taxes                        | 172.9                       | 163.1                       |
| Dividends payable                                    | 34.0                        | 31.1                        |
| Income taxes                                         | 228.9                       | 135.0                       |
| <b>Total current liabilities</b>                     | <b>2,520.8</b>              | <b>2,176.4</b>              |
| <br>                                                 |                             |                             |
| Obligations under Capital Leases                     | 1,822.3                     | 1,824.4                     |
| Long-Term Debt                                       | 711.2                       | 596.0                       |
| Other Long-Term Liabilities                          | 127.8                       | 94.0                        |
| Deferred Income Taxes                                | 60.9                        | 51.6                        |
| <br>                                                 |                             |                             |
| <b>Shareholders' Equity:</b>                         |                             |                             |
| Common stock                                         | 125.9                       | 124.5                       |
| Capital in excess of par value                       | 293.4                       | 271.9                       |
| Income retained for use in the business              | 2,569.1                     | 2,204.9                     |
| Cumulative foreign currency translation adjustment   | (48.3)                      |                             |
| <b>Total shareholders' equity</b>                    | <b>2,940.1</b>              | <b>2,601.3</b>              |
|                                                      | <b>\$8,183.1</b>            | <b>\$7,343.7</b>            |

# CONSOLIDATED STATEMENTS OF CHANGES IN FINANCIAL POSITION

| (Millions)                                                                                                                                                                   | Fiscal Year Ended   |                     |                     |
|------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|---------------------|---------------------|---------------------|
|                                                                                                                                                                              | January 25,<br>1984 | January 26,<br>1983 | January 27,<br>1982 |
| <b>Cash Provided by (Used for):</b>                                                                                                                                          |                     |                     |                     |
| <i>Operations</i>                                                                                                                                                            |                     |                     |                     |
| Net income for the year                                                                                                                                                      | \$492.3             | \$261.8             | \$220.3             |
| Noncash charges (credits) to earnings—                                                                                                                                       |                     |                     |                     |
| Depreciation and amortization:                                                                                                                                               |                     |                     |                     |
| Property owned                                                                                                                                                               | 167.8               | 157.4               | 140.7               |
| Leased property under capital leases                                                                                                                                         | 96.7                | 93.7                | 88.9                |
| Provision for store closings                                                                                                                                                 |                     | 44.5                |                     |
| Deferred income taxes                                                                                                                                                        | 21.5                | 7.6                 | 11.8                |
| Equity in undistributed income of affiliated retail companies and insurance operations                                                                                       | (16.8)              | (15.9)              | (16.5)              |
| Increase in other long-term liabilities                                                                                                                                      | 33.8                | 21.2                | 19.1                |
| Other                                                                                                                                                                        | .8                  | 6.4                 | 5.5                 |
| Total from net income                                                                                                                                                        | 796.1               | 576.7               | 469.8               |
| Cash provided by (used for) current assets and current liabilities—                                                                                                          |                     |                     |                     |
| Increase in inventories                                                                                                                                                      | (286.7)             | (159.8)             | (289.2)             |
| Increase in accounts payable                                                                                                                                                 | 203.8               | 260.4               | 192.8               |
| Net change in other current assets and other current liabilities                                                                                                             | 106.6               | 130.2               | (95.3)              |
| Net cash provided by operations                                                                                                                                              | 819.8               | 807.5               | 278.1               |
| <i>Financing</i>                                                                                                                                                             |                     |                     |                     |
| Increase in long-term debt and notes payable                                                                                                                                 | 123.4               | 197.2               | 168.2               |
| Reduction in long-term debt and notes payable                                                                                                                                | (10.4)              | (181.4)             | (4.0)               |
| Obligations incurred under capital leases                                                                                                                                    | 78.9                | 141.8               | 197.9               |
| Reduction in capital lease obligations                                                                                                                                       | (75.5)              | (63.0)              | (59.1)              |
| Sale of common stock under stock option, purchase and employees' savings plans and conversion of debentures (includes \$5.4 for acquisition of Bishop Buffets, Inc. in 1983) | 22.9                | 8.2                 | 11.0                |
| Net cash provided by financing                                                                                                                                               | 139.3               | 102.8               | 314.0               |
| <i>Dividends Paid</i>                                                                                                                                                        | (132.2)             | (123.0)             | (117.5)             |
| <i>Investments</i>                                                                                                                                                           |                     |                     |                     |
| Property additions—                                                                                                                                                          |                     |                     |                     |
| Property owned (includes \$10.0 in 1983 relating to acquisition of Bishop Buffets, Inc.)                                                                                     | (377.9)             | (306.4)             | (361.4)             |
| Leased property under capital leases                                                                                                                                         | (37.8)              | (85.0)              | (178.2)             |
| Proceeds from the sale of property                                                                                                                                           | 91.4                | 49.7                | 38.2                |
| Increase in investments in and advances to affiliated retail companies and insurance operations                                                                              | (24.5)              | (3.8)               | (68.2)              |
| Other—net                                                                                                                                                                    | (4.2)               | (3.2)               | (2.8)               |
| Net cash used for investments                                                                                                                                                | (353.0)             | (348.7)             | (572.4)             |
| <b>Net Increase (Decrease) in Cash and Temporary Investments</b>                                                                                                             | <b>\$473.9</b>      | <b>\$438.6</b>      | <b>\$(97.8)</b>     |

See Notes to Consolidated Financial Statements.

# NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

## (A) Summary of Significant Accounting Policies

**Fiscal Year:** The company's fiscal year ends on the last Wednesday in January. Fiscal years 1983, 1982 and 1981 all consisted of 52 weeks and ended on January 25, 1984, January 26, 1983 and January 27, 1982, respectively.

**Basis of Consolidation:** The company includes all majority-owned retail subsidiaries in the consolidated financial statements. The accounts of Furr's Cafeterias, Inc. and Bishop Buffets, Inc. are included in the consolidated financial statements on the basis of fiscal years generally ending on December 31. Investments in affiliated retail companies owned 20% or more and the wholly owned insurance operations are accounted for by the equity method using their December financial statements. All significant intercompany transactions and accounts have been eliminated in consolidation.

**Foreign Operations:** Under Financial Accounting Standard No. 52, "Foreign Currency Translation," adopted in fiscal 1983, foreign currency assets and liabilities are translated into U.S. dollars at the exchange rates in effect at the balance sheet date except for operations in countries with high inflation. Results of operations are translated at average exchange rates during the period for revenue and expenses. Except for operations in countries with high inflation, translation gains and losses resulting from fluctuations in the exchange rates are accumulated as a separate component of shareholders' equity. [See Note (B).] Prior to 1983, inventories, owned property, leased property and the related depreciation and amortization and all other noncurrent assets were translated at historical exchange rates. Exchange gains or losses were included in net income.

**Inventories:** Merchandise inventories are valued at the lower of cost or market, using the retail method, on the last-in, first-out basis for substantially all domestic inventories and the first-in, first-out basis for the remainder.

**Property Owned:** Land, buildings, leasehold improvements and equipment are recorded at cost. Major replacements and refurbishings are charged to the property accounts while replacements, maintenance and repairs which do not improve or extend the life of the respective assets are expensed currently. The company capitalizes interest cost as part of the cost of constructing capital assets.

The cost of all properties retired and the accumulated depreciation thereon are eliminated from the accounts and

the resulting gain or loss is taken into income. Prior to 1982, the cost of ordinary retirements was charged to the allowance for depreciation. The effect of this change was not material in relation to the consolidated financial statements.

**Depreciation:** The company computes depreciation on owned property principally on the straight-line method for financial statement purposes. For income tax purposes the accelerated cost recovery system is used for assets placed in service after 1980 and accelerated depreciation methods are used for assets placed in service in 1980 and prior years. Most store properties are leased, and improvements are amortized over the term of the lease but not more than 25 years. Other annual rates used in computing depreciation for financial statement purposes are 2% to 10% for buildings, 10% to 14% for store fixtures and 5% to 33% for other fixtures and equipment.

**Leased Property under Capital Leases:** The company accounts for capital leases, which transfer substantially all of the benefits and risks incident to the ownership of property, as an acquisition of an asset and the incurrence of an obligation. Under this method of accounting for leases, the asset is amortized using the straight-line method and the obligation, including interest thereon, is liquidated over the life of the lease. All other leases (operating leases) are accounted for by recording periodic rental expense over the life of the lease.

**Licensee Sales:** The company's policy is to exclude sales of licensed departments from total sales.

**Preopening and Closing Costs:** The company follows the practice of treating store operating costs incurred prior to opening a new retail unit as current period expenses. When the decision to close a retail unit is made, the company provides for future estimated costs, including future net lease obligations, nonrecoverable investments in fixed assets, other expenses directly related to discontinuance of operations and estimated operating losses through expected closing dates.

**Income Taxes:** Deferred income taxes are provided on nonpermanent differences between financial statement and taxable income.

The company accrues appropriate U.S. and foreign taxes payable upon all of the earnings of subsidiaries and affiliates, except with respect to earnings that are intended

to be permanently reinvested. Any additional taxes or credits related to subsequent distributions of such earnings are determined and taken into account at the time of distribution.

**Investment Credit:** The company uses the "flow through" method of accounting for investment credit whereby income tax expense is reduced for the period in which expenditures create the tax benefit.

### (B) Accounting Change

The company changed its method of accounting for foreign currency translation in fiscal 1983 by adopting Financial Accounting Standard No. 52 ("FAS 52"). Prior years' financial statements have not been restated because the impact was not material. The foreign currency translation adjustment of \$39.6 million at January 27, 1983, resulting from the application of the new requirements to the January 26, 1983 balance sheet, is shown below as the beginning balance of the cumulative foreign currency translation adjustment account.

An analysis of changes in the cumulative foreign currency translation adjustment account included in shareholders' equity for the year ended January 25, 1984 follows:

| (Millions)                                                                   |          |
|------------------------------------------------------------------------------|----------|
| Beginning balance, January 27, 1983                                          | \$(39.6) |
| Translation adjustments for the year, net of applicable income taxes of \$.1 | (8.7)    |
| Balance at January 25, 1984                                                  | \$(48.3) |

### (C) Store Closings

During 1982, the company made a thorough review of operations which resulted in a determination that a number of stores and auto service departments were operating at unacceptable levels of profitability. Following this review process, the company closed eight Kmart stores, a total of 66 Kresge and Jupiter stores, 361 automotive service departments and planned a phaseout of 17 additional Kmart stores in 1983 resulting in a pretax provision of \$44.5 million (\$.19 per share after tax) in 1982.

### (D) Acquisitions

On December 20, 1983, Kmart Corporation issued 761,840 shares of common stock, through a wholly owned subsidiary, for all of the common shares of Bishop Buffets, Inc. ("Bishop"). Bishop operates a chain of cafeterias in eight midwestern and western states. The acquisition has been accounted for as a pooling of interests; however, the

financial statements have not been restated for periods prior to the acquisition due to immateriality.

On September 4, 1981, the company acquired, for \$50.0 million in cash, 44% of Astra, S.A. ("Astra"), which was previously a wholly owned retailing subsidiary of the Gentor Group of Monterrey, Mexico. Astra is a holding company of certain Mexican companies which primarily operate retail food and general merchandise stores in Mexico. Excess of cost over acquired net assets of approximately \$33.0 million is being amortized over a 40-year period under the straight-line method. The investment is accounted for using the equity method and accordingly, the company's equity in Astra's financial results since the acquisition date is included in income. Astra's results of operations prior to the date of acquisition are not material in relation to the consolidated financial statements.

### (E) Merchandise Inventories

A summary of inventories by method of pricing and the excess of current cost over stated LIFO value follows:

| (Millions)                                        | January 25,<br>1984 | January 26,<br>1983 |
|---------------------------------------------------|---------------------|---------------------|
| Last-in, first-out (cost not in excess of market) | \$3,108.0           | \$2,875.8           |
| Lower of cost (first-in, first-out) or market     | 473.6               | 419.1               |
| Total                                             | \$3,581.6           | \$3,294.9           |
| Excess of current cost over stated LIFO value     | \$ 526.6            | \$ 481.0            |

### (F) Equity Company Information

All U.S. Kmart footwear departments are operated under license agreements with the Meldisco subsidiaries of the Melville Corporation, substantially all of which are 49% owned by the company and 51% owned by Melville. Fees and income earned under the license agreements in 1983, 1982 and 1981 of \$137.4 million, \$117.3 million and \$102.4 million, respectively, are included in licensee fees and rental income. The company's equity in the income of these operations and dividends received in 1983, 1982 and 1981 were as follows:

| (Millions)                              | 1983   | 1982   | 1981   |
|-----------------------------------------|--------|--------|--------|
| Equity in income of Meldisco operations | \$40.2 | \$31.9 | \$27.7 |
| Dividends                               | \$33.3 | \$26.6 | \$25.0 |

Melisco subsidiaries' summarized financial information follows:

| (Millions)   | Year Ended December 31, |         |         |
|--------------|-------------------------|---------|---------|
|              | 1983                    | 1982    | 1981    |
| Net sales    | \$848.4                 | \$759.3 | \$688.6 |
| Gross profit | \$364.9                 | \$312.1 | \$277.1 |
| Net income   | \$ 83.1                 | \$ 66.2 | \$ 57.2 |

| (Millions)                  | December 31, |         |         |
|-----------------------------|--------------|---------|---------|
|                             | 1983         | 1982    | 1981    |
| Inventory                   | \$ 94.9      | \$ 90.6 | \$ 83.8 |
| Other current assets        | 102.5        | 75.6    | 64.5    |
| Noncurrent assets           | 2.8          | 3.4     | 3.9     |
| Total assets                | 200.2        | 169.6   | 152.2   |
| Current liabilities         | 42.3         | 27.1    | 22.0    |
| Net assets                  | \$157.9      | \$142.5 | \$130.2 |
| Equity of Kmart Corporation | \$ 76.3      | \$ 68.7 | \$ 62.7 |

The company has a 20% equity interest in G. J. Coles & Coy. Limited ("Coles"), the major food and general-merchandise retailer in Australia. Income earned under the Kmart license agreement in 1983, 1982 and 1981 of \$2.4 million, \$2.5 million and \$2.3 million, respectively, is included in licensee fees and rental income. The company's equity in the income of Coles' operations, dividends, year-end investment in Coles and the market value of Coles' common stock owned by the company follows. As a result of translating the company's equity in the investment of Coles according to FAS 52, the equity of Kmart Corporation was reduced by \$31.4 million in 1983.

| (Millions U.S. \$)                  | 1983    | 1982    | 1981    |
|-------------------------------------|---------|---------|---------|
| Equity in income                    | \$ 17.2 | \$ 21.6 | \$ 19.3 |
| Dividends                           | \$ 6.7  | \$ 7.0  | \$ 7.5  |
| Equity of Kmart Corporation         | \$102.8 | \$109.2 | \$ 94.6 |
| Market value of Coles' common stock | \$176.9 | \$103.4 | \$105.4 |

Summarized financial information adjusted for conformity with U.S. generally accepted accounting principles for Coles' most recent fiscal years follows. Information presented for 1983 was translated into U.S. dollars under the principles of FAS 52. [See Note (B).] For 1982 and 1981, the financial statements were translated according to FAS 8.

| (Millions U.S. \$) | Fiscal Year Ended July, |           |           |
|--------------------|-------------------------|-----------|-----------|
|                    | 1983                    | 1982      | 1981      |
| Net sales          | \$4,404.7               | \$4,423.6 | \$3,759.7 |
| Net income         | \$ 73.0                 | \$ 70.2   | \$ 70.2   |

| (Millions U.S. \$)           | July, 1983 | July, 1982 | July, 1981 |
|------------------------------|------------|------------|------------|
| Current assets               | \$ 471.6   | \$ 449.5   | \$ 460.4   |
| Noncurrent assets            | 922.6      | 974.8      | 802.4      |
| Total assets                 | \$1,394.2  | \$1,424.3  | \$1,262.8  |
| Current liabilities          | \$ 533.1   | \$ 535.9   | \$ 479.3   |
| Noncurrent liabilities       | 340.5      | 313.4      | 295.8      |
| Equity                       | 520.6      | 575.0      | 487.7      |
| Total liabilities and equity | \$1,394.2  | \$1,424.3  | \$1,262.8  |

Kmart Insurance Services, Inc. summarized financial information with respect to insurance operations follows:

| (Millions)               | Year Ended December 31, |         |         |
|--------------------------|-------------------------|---------|---------|
|                          | 1983                    | 1982    | 1981    |
| Premium and other income | \$112.9                 | \$ 95.7 | \$ 71.2 |
| Costs and expenses       | 107.8                   | 90.8    | 66.6    |
| Net income               | \$ 5.1                  | \$ 4.9  | \$ 4.6  |

| (Millions)                                | December 31, |         |         |
|-------------------------------------------|--------------|---------|---------|
|                                           | 1983         | 1982    | 1981    |
| Cash and receivables                      | \$ 18.4      | \$ 9.2  | \$ 11.7 |
| Investments                               | 173.9        | 160.0   | 141.7   |
| Policy acquisition costs and other assets | 99.6         | 80.1    | 65.4    |
| Total assets                              | 291.9        | 249.3   | 218.8   |
| Policy and claim reserves                 | 136.2        | 119.0   | 103.7   |
| Other liabilities                         | 27.1         | 16.0    | 15.5    |
| Equity of Kmart Corporation               | \$128.6      | \$114.3 | \$ 99.6 |

Unremitted earnings of unconsolidated subsidiaries included in consolidated retained earnings were \$112.9 million at January 25, 1984.

### (G) Compensating Balances

At January 25, 1984, the company had bank lines of credit aggregating \$803.6 million with interest rates approximating the "prime" lending rate. In support of certain lines of credit, it is expected that compensating balances will be maintained on deposit with the banks, which will average 10% of the line to the extent that it is not in use and an additional 10% on the portion in use, whereas other lines require fees in lieu of compensating balances. The company is free to withdraw the entire balance in its accounts at any time.

## (H) Estimated Income Taxes

The effective income tax rate is reconciled to the Federal statutory rate as follows:

| (Millions)                                                                 | Fiscal Year Ended   |                     |                     |
|----------------------------------------------------------------------------|---------------------|---------------------|---------------------|
|                                                                            | January 25,<br>1984 | January 26,<br>1983 | January 27,<br>1982 |
| Income before estimated income taxes:                                      |                     |                     |                     |
| U.S.                                                                       | \$828.3             | \$397.8             | \$296.1             |
| Foreign                                                                    | 25.4                | 21.1                | 26.8                |
| Total                                                                      | \$853.7             | \$418.9             | \$322.9             |
| Tax thereon, computed at statutory rate of 46%                             | \$392.7             | \$192.7             | \$148.5             |
| Increases (reductions) in taxes resulting from:                            |                     |                     |                     |
| State and local income taxes net of federal income tax benefit             | 19.6                | 11.1                | 9.2                 |
| Tax credits (1983 includes a \$4.1 PAYSEP tax credit)                      | (25.6)              | (19.6)              | (28.4)              |
| Equity in income of affiliated retail companies subject to lower tax rates | (23.3)              | (21.8)              | (18.6)              |
| Other                                                                      | 3.1                 | (.4)                | (3.5)               |
| Estimated income taxes                                                     | \$366.5             | \$162.0             | \$107.2             |
| Effective rate                                                             | 42.9%               | 38.7%               | 33.2%               |
| Tax effects of timing differences:                                         |                     |                     |                     |
| Accelerated depreciation                                                   | \$ 19.3             | \$ 24.8             | \$ 32.4             |
| Capitalized leases                                                         | (14.2)              | (14.9)              | (14.5)              |
| Provision for store closings                                               |                     | (18.7)              |                     |
| Other                                                                      | 16.4                | 16.4                | (6.1)               |
| Total                                                                      | \$ 21.5             | \$ 7.6              | \$ 11.8             |

The amounts shown on the balance sheets for deferred income taxes result principally from the difference between financial statement and income tax depreciation, reduced by the effect of accounting for certain leases as capital leases of \$125.6 million at January 25, 1984. The net amount of current deferred taxes at January 25, 1984 was \$8.6 million, which relates principally to LIFO, layaways and the timing difference in certain taxes and is included in income taxes payable. At January 26, 1983, the net amount of current prepaid deferred taxes was \$3.6 million, which related to the current portion of accrued employee benefits and uninsured claims and was included in operating supplies and prepaid expenses.

Undistributed earnings of subsidiaries, which are intended to be permanently reinvested, totaled \$182.1 million at January 25, 1984.

## (I) Long-Term Debt

| (Millions)                                                                      | January 25,<br>1984 | January 26,<br>1983 |
|---------------------------------------------------------------------------------|---------------------|---------------------|
| 9½% notes due 1985 (net of unamortized discount of \$.4 and \$.7, respectively) | \$199.6             | \$199.3             |
| 6% convertible subordinated debentures due 1999                                 | 199.3               | 199.9               |
| Commercial paper and notes payable to banks                                     | 300.0               | 179.3               |
| Other                                                                           | 15.5                | 22.6                |
|                                                                                 | 714.4               | 601.1               |
| Portion due within one year                                                     | 3.2                 | 5.1                 |
| Total long-term debt                                                            | \$711.2             | \$596.0             |

The 9½% notes due July 15, 1985 are unsecured obligations of the company and may be redeemed at a price equal to 100% of the principal amount plus accrued interest.

The debentures due 1999 are convertible into common stock at \$35.50 per share. The indenture relating to the debentures provides that the company shall pay \$11.0 million into a sinking fund on July 15 each year from 1985 to 1998, inclusive. The debentures are subject to redemption through the sinking fund at 100% of the principal amount, or at any time at the option of the company at prices declining from 106% to 100% of the principal amount after July 15, 1994. At January 25, 1984, a total of 5,614,739 shares of authorized common stock are reserved for conversion.

The company entered into revolving credit agreements with various banks in the aggregate amount of \$180.0 million in 1982, and an additional \$120.0 million in 1983. The agreements, which are for terms of either three or five years, provide for borrowings at an interest rate based on the prime rate, "CD-based rate," or "LIBOR-based rate" at the company's election. As of January 25, 1984, the company had no outstanding borrowings under these agreements. At January 25, 1984 and January 26, 1983, these agreements support \$300.0 million and \$179.3 million, respectively, of commercial paper and notes payable to banks that have been classified as long-term debt based on the company's intention to maintain at least that amount of similar debt outstanding during the next year.

Certain of the long-term debt agreements contain covenants regarding the maintenance of net worth, working capital, coverage ratios and payment of cash dividends. Retained earnings at January 25, 1984 exceed the terms of the most restrictive of these agreements by \$923.3 million.

Principal payments on long-term debt (excluding \$300.0 million in commercial paper and notes payable to banks classified as long-term debt for 1983) for the five years subsequent to 1983, in millions, are: 1984-\$3.2; 1985-\$212.8; 1986-\$15.4; 1987-\$11.8; 1988-\$11.4.

## (J) Leases

**Description of Leasing Arrangements:** The company conducts operations primarily in leased facilities. Store leases are generally for terms of 25 years with multiple five-year renewal options which allow the company the option to extend the life of the lease up to 50 years beyond the initial noncancellable term. Certain leases provide for additional rental payments based on sales volume in excess of a specified base. Also, certain leases provide for the payment by the lessee of executory costs (taxes, maintenance and insurance), and selling space has been sublet to other retailers in certain of the company's leased facilities.

**Lease Commitments:** Future minimum lease payments with respect to capital and operating leases are:

| (Millions)                                                                     | Minimum<br>Lease Payments |           |
|--------------------------------------------------------------------------------|---------------------------|-----------|
|                                                                                | Capital                   | Operating |
| Fiscal Year:                                                                   |                           |           |
| 1984                                                                           | \$ 341.4                  | \$ 214.5  |
| 1985                                                                           | 337.4                     | 211.3     |
| 1986                                                                           | 331.6                     | 207.0     |
| 1987                                                                           | 325.4                     | 203.0     |
| 1988                                                                           | 320.4                     | 196.3     |
| Later years                                                                    | 4,175.9                   | 2,430.6   |
| Total minimum lease payments                                                   | 5,832.1                   | 3,462.7   |
| Less—minimum sublease rental income                                            |                           | (160.5)   |
| Net minimum lease payments                                                     | 5,832.1                   | \$3,302.2 |
| Less:                                                                          |                           |           |
| Amount representing estimated<br>executory costs                               | (1,591.7)                 |           |
| Amount representing interest                                                   | (2,347.5)                 |           |
| Obligations under capital leases,<br>of which \$70.6 is due within<br>one year | \$1,892.9                 |           |

The company has guaranteed indebtedness related to certain leased properties financed by industrial revenue bonds. As of January 25, 1984, the total amount of such guaranteed indebtedness is \$280.3 million, of which \$119.6 million is included in capital lease obligations.

**Rental Expense:** A summary of operating lease rental expense and short-term rentals follows:

| (Millions)                       | Fiscal Year Ended   |                     |                     |
|----------------------------------|---------------------|---------------------|---------------------|
|                                  | January 25,<br>1984 | January 26,<br>1983 | January 27,<br>1982 |
| Minimum rentals                  | \$227.5             | \$202.2             | \$183.3             |
| Rentals based on sales<br>volume | 38.4                | 32.2                | 33.3                |
| Less—sublease rentals            | (35.5)              | (33.5)              | (32.6)              |
| Total                            | \$230.4             | \$200.9             | \$184.0             |

**Reconciliation of Capital Lease Information:** Capital lease amortization and interest charged to operations are reconciled to minimum capital lease payments as follows:

| (Millions)                                                                                                                                  | Fiscal Year Ended   |                     |                     |
|---------------------------------------------------------------------------------------------------------------------------------------------|---------------------|---------------------|---------------------|
|                                                                                                                                             | January 25,<br>1984 | January 26,<br>1983 | January 27,<br>1982 |
| Amortization of leased<br>property under capital<br>leases                                                                                  | \$ 96.7             | \$ 93.7             | \$ 88.9             |
| Interest expense related<br>to obligations under<br>capital leases                                                                          | 189.0               | 176.5               | 160.8               |
| Amounts charged to<br>earnings                                                                                                              | 285.7               | 270.2               | 249.7               |
| Related minimum lease<br>payments (excluding<br>executory costs in 1983,<br>1982 and 1981 of \$76.7,<br>\$73.6 and \$67.3,<br>respectively) | (255.1)             | (239.4)             | (219.9)             |
| Excess of amounts charged<br>over related minimum<br>lease payments                                                                         | \$ 30.6             | \$ 30.8             | \$ 29.8             |

In 1983, there were no currency gains or losses recognized from the inclusion of capital leases for foreign operations due to the adoption of FAS 52. [See Note (B).] The inclusion of capital leases of foreign operations increased currency fluctuation gains by \$3.0 million in 1982 and reduced currency fluctuation gains by \$1.1 million in 1981.

## (K) Segment and Geographic Information

The dominant portion of the company's operations is in a single industry, retailing general merchandise through the operation of a chain of discount department stores.

The company has both domestic and foreign operations, which are summarized as follows:

| (Millions U.S. \$)                       | 1983       | 1982       | 1981       |
|------------------------------------------|------------|------------|------------|
| Sales:                                   |            |            |            |
| U.S.                                     | \$17,785.7 | \$16,007.1 | \$15,752.3 |
| Canada                                   | 812.2      | 765.1      | 774.7      |
| Total                                    | \$18,597.9 | \$16,772.2 | \$16,527.0 |
| Licenses fees and other income:          |            |            |            |
| U.S.                                     | \$ 258.1   | \$ 240.9   | \$ 216.9   |
| Canada                                   | 3.3        | 3.7        | 3.2        |
| Australia                                | 19.6       | 24.0       | 21.6       |
| Total                                    | \$ 281.0   | \$ 268.6   | \$ 241.7   |
| Income from retail operations:           |            |            |            |
| U.S.                                     | \$ 459.7   | \$ 229.2   | \$ 191.0   |
| Canada                                   | 9.4        | 4.5        | 4.6        |
| Australia                                | 18.1       | 23.2       | 20.1       |
|                                          | 487.2      | 256.9      | 215.7      |
| Equity in income of insurance operations | 5.1        | 4.9        | 4.6        |
| Net income for the year                  | \$ 492.3   | \$ 261.8   | \$ 220.3   |
| Identifiable assets:                     |            |            |            |
| U.S.                                     | \$ 7,497.6 | \$ 6,642.0 | \$ 5,982.9 |
| Canada                                   | 345.1      | 371.1      | 364.1      |
|                                          | 7,842.7    | 7,013.1    | 6,347.0    |
| Investments in and advances to:          |            |            |            |
| Affiliated retail companies—             |            |            |            |
| U.S.                                     | 76.3       | 68.7       | 62.7       |
| Australia                                | 102.8      | 109.2      | 94.6       |
| Mexico                                   | 32.7       | 38.4       | 53.4       |
| Insurance operations                     | 128.6      | 114.3      | 99.6       |
| Total assets                             | \$ 8,183.1 | \$ 7,343.7 | \$ 6,657.3 |

Operating results of certain foreign operations, which are not significant, are included in U.S. amounts.

The company's equity in income in G. J. Coles & Coy. Limited ("Coles") of Australia and license fees from Coles are included under the caption "Licensee fees and other income." [See Note (F).]

In 1983, due primarily to the adoption of FAS 52, currency gains or losses included in income from retail operations were insignificant. [See Note (B).] Currency fluctuations, which are included in income from retail operations for 1982 and 1981, reflect the effect of exchange rate changes recognized when financial statements of foreign operations are translated into U.S. dollars. Currency fluctuations, including net amounts reported in Australian and Mexican equity income, consisted of gains of \$3.7 million in 1982 and \$1.2 million in 1981.

Identifiable assets are those assets of the company that are identified with operations in a specific geographic area. Corporate assets (assets which are used by two or more geographic operations) and transfers between geographic areas are insignificant.

### (L) Shareholders' Equity

Changes in shareholders' equity other than income retained for use in the business for the three fiscal years ended January 25, 1984, and the cumulative foreign currency translation adjustment for 1983 were as follows:

| (\$ in Millions)                                                                               | Common Stock<br>(Authorized 250,000,000 Shares<br>\$1.00 Par Value) |         |  | Capital in<br>Excess of<br>Par Value |
|------------------------------------------------------------------------------------------------|---------------------------------------------------------------------|---------|--|--------------------------------------|
|                                                                                                | Shares<br>Outstanding                                               | Amount  |  |                                      |
| Balance January 28, 1981                                                                       | 123,378,601                                                         | \$123.4 |  | \$253.8                              |
| Common stock sold under stock option and purchase plans and conversion of debentures           | 597,785                                                             | .6      |  | 10.4                                 |
| Balance January 27, 1982                                                                       | 123,976,386                                                         | 124.0   |  | 264.2                                |
| Common stock sold under stock option and purchase plans and conversion of debentures           | 517,960                                                             | .5      |  | 7.7                                  |
| Balance January 26, 1983                                                                       | 124,494,346                                                         | 124.5   |  | 271.9                                |
| Common stock issued for acquisition of Bishop Buffets, Inc.                                    | 761,840                                                             | .8      |  | 4.6                                  |
| Common stock sold under stock option and employees' savings plans and conversion of debentures | 654,619                                                             | .6      |  | 16.9                                 |
| Balance January 25, 1984                                                                       | 125,910,805                                                         | \$125.9 |  | \$293.4                              |

Ten million shares of no par value preferred stock with voting and cumulative dividend rights are authorized but unissued. Currently, there are no plans for its issuance.

At January 25, 1984, there were 15,918,064 shares of common stock reserved for possible issuance under the company's Stock Option Plans, Employees' Savings Plan and for conversion of the 6% convertible subordinated debentures.

**(M) Earnings Per Common and Common Equivalent Share**  
Earnings per common and common equivalent share were computed by dividing net income by the weighted average number of shares of common stock and dilutive common stock equivalents outstanding during each year. In making the computation for 1983, 1982 and 1981, common shares at the beginning of the year were increased by the number of shares issuable on conversion of the 6% convertible debentures (issued in 1974) and net income was adjusted for interest expense net of the related tax effect. The number of common shares was increased by the number of shares issuable under the Stock Purchase Incentive Plan (1982 and 1981 only) and the Stock Option Plans, less the number of shares that were assumed to have been purchased at average market prices with the proceeds of sales under the plans. The shares issued in 1983 for the pooling of interests with Bishop Buffets, Inc. were not assumed to be outstanding prior to the date of acquisition because net income prior to date of acquisition was not restated due to immateriality. [See Note (D).]

#### **(N) Pension Plans**

The company and its subsidiaries have noncontributory pension plans covering most employees. Total pension expense was \$42.2 million for 1983, \$42.7 million for 1982 and \$40.8 million for 1981. In 1983, the effect of a change in the assumed rate of employee turnover based on the company's actual experience decreased pension expense by \$6.0 million. The effect of the change was offset by a general increase in pension costs in 1983. The company's policies are to fund pension costs accrued and to amortize prior service costs principally over 30 years.

A comparison of accumulated benefits and net assets for the company's principal pension plan as of the most recent valuation dates follows:

| (Millions)                                               | January 26,<br>1983 | January 27,<br>1982 |
|----------------------------------------------------------|---------------------|---------------------|
| Actuarial present value of<br>accumulated plan benefits: |                     |                     |
| Vested                                                   | \$269.8             | \$222.8             |
| Nonvested                                                | 82.2                | 77.0                |
| Total                                                    | \$352.0             | \$299.8             |
| Net assets available for benefits                        | \$475.4             | \$353.7             |

The weighted average assumed rate of return used in determining the actuarial value of accumulated plan benefits was 7.0% for both years.

#### **(O) Employees' Savings, Stock Option and Stock Purchase Incentive Plans**

Information on these plans is summarized below:

##### **Employees' Savings Plan**

The Employees' Savings Plan (the "Savings Plan"), which commenced July 1, 1982 and was amended effective October 1, 1983, provides that employees of the company and certain subsidiaries who have completed two "years of service" can invest from 2% to 12% of their earnings in the employees' choice of a diversified common stock fund, an insured guaranteed investment fund or a Kmart common stock fund. For each dollar the employee invests up to 6% of his or her earnings, the company will contribute an additional 50 cents, which is invested in the Kmart common stock fund. Contributions for the Kmart common stock fund may be remitted to the Trustee in whole or in part in the form of company common stock.

As of September 1, 1983, 2,000,000 shares of Kmart common stock were made available for issuance or sale to the Trustee. As of January 25, 1984, 1,790,865 shares were available for sale. Under the terms of the agreement, contributions remitted to the Trustee may be used to acquire Kmart common stock pursuant to market purchases or directly from the company by subscription or purchase. The company's expense related to the Savings Plan, which includes only a partial year for 1982, was \$25.5 million for 1983 and \$13.2 million for 1982.

As part of the amended Savings Plan, effective October 1, 1983, the company added a Payroll-Based Stock Ownership Plan ("PAYSOP"). Under the PAYSOP provisions, the company makes a contribution for all employees eligible for the Savings Plan, to be invested in the Kmart common stock fund, based on ½% of taxable compensation paid in fiscal 1983. The company will receive a direct income tax credit for 1983 in the amount of the PAYSOP contribution.

### Stock Option Plans

|                                                                   | Number of Shares |           |
|-------------------------------------------------------------------|------------------|-----------|
|                                                                   | 1983             | 1982      |
| Available for grant at beginning of year                          | 6,130,985        | 418,805   |
| Under option at beginning of year (\$19.31 to \$37.63 per share)  | 2,854,400        | 2,569,680 |
| Additional shares made available for grant                        |                  | 6,000,000 |
| Options:                                                          |                  |           |
| Granted (\$32.81 to \$35.75 per share)                            | 1,235,300        | 411,600   |
| Exercised (\$19.31 to \$34.94 per share)                          | 472,925          | 3,100     |
| Cancelled (\$19.31 to \$37.63 per share)                          | 457,385          | 123,780   |
| Under option at end of year (\$19.31 to \$35.75 per share)        | 3,159,390        | 2,854,400 |
| Options exercisable at end of year (\$19.31 to \$34.94 per share) | 1,948,490        | 2,447,000 |
| Available for grant at end of year                                | 5,353,070        | 6,130,985 |

Under the company's 1973 Stock Option Plan (the "1973 Plan"), which was approved by shareholders in June 1973 and amended in 1978, 1980, 1981 and 1982, options to acquire up to 4,000,000 shares of common stock may be granted to officers and key employees at no less than 100% of the fair market value on the date of grant.

Options under the 1973 Plan may have a maximum term of ten years and are exercisable two years after the date of grant, except that the two-year limitation does not apply if employment terminates due to total and permanent disability or death. Payment upon exercise of an option may be made in cash, already-owned shares or a combination of both. Such shares will be valued at their fair market value as of the date of exercise.

The 1973 Plan provides for stock appreciation rights ("SARs") in tandem with nonqualified stock options for officers and eligible directors who are limited under the Securities Exchange Act of 1934 in dealing with shares of the company's stock. The 1973 Plan provides that such an optionee may request that the Compensation and

Incentives Committee permit the optionee to surrender all or part of an exercisable option in return for stock, cash or a combination of both equal to any appreciation in the value of the surrendered shares over the option price. Compensation expense is recorded to the extent that the market price of the option exceeds the grant price. Compensation expense was \$2.2 million in 1983, \$8 million in 1982 and none in 1981.

Under the terms of the 1981 Incentive Stock Option Plan (the "1981 Plan"), which was approved by shareholders in May 1982, options to acquire up to 5,000,000 shares of common stock may be granted to officers and other key employees of the company at no less than 100% of the fair market value on the date of grant. Options under the 1981 Plan are intended to be incentive stock options ("ISOs") pursuant to Section 422A of the Internal Revenue Code. Such options may have a maximum term of ten years and are exercisable two years after the date of grant, except that an ISO may not be exercised by an optionee who has a prior ISO outstanding. Payment upon exercise of an option may be made in cash, already-owned shares or a combination of both. Such shares will be valued at their fair market value as of the date of exercise. SARs do not apply to ISOs under the 1981 Plan.

### Stock Purchase Incentive Plan

Under the Stock Purchase Incentive Plan, which terminated June 30, 1982, employees of the company or of certain subsidiaries who had completed one year of service were eligible to purchase up to 4,500,000 shares of common stock through June 1982, at the lower of 85% of market value on the first or last day of each plan year. Of the 1,732,954 shares available for purchase at January 27, 1982, 514,382 shares were purchased during 1982 through payroll deductions at \$15.62 per share.

### (P) Contingent Obligations

On January 29, 1982, Astra, S.A. ("Astra"), the company's Mexican retail affiliate, made a public offering of long-term debt in the principal amount of \$100.0 million to finance the acquisition of land and the construction and fixturing of new Astra discount department and food stores in Mexico. The 16¾% notes due 1992 are unconditionally guaranteed by K mart Corporation. The company has additionally guaranteed a bank loan of \$12.0 million.

The company and G. J. Coles & Coy. Limited ("Coles") have guaranteed indebtedness related to certain properties in Australia on a joint and several basis. Coles subsequently indemnified K mart Corporation from any liability incurred pursuant to its guarantees. As of January 25, 1984, the amount guaranteed was \$48.6 million. [See Note (F).]

**(Q) Quarterly Financial Information (Unaudited)**

Each of the quarters includes 13 weeks.

**Consolidated Statements of Income\***

| (Millions)                                             | Quarter        |                 |                |                 |
|--------------------------------------------------------|----------------|-----------------|----------------|-----------------|
|                                                        | First          | Second          | Third          | Fourth          |
| <b>1983</b>                                            |                |                 |                |                 |
| Sales                                                  | \$3,934.6      | \$4,679.4       | \$4,331.7      | \$5,652.2       |
| Licensee fees and other income                         | 43.2           | 57.2            | 54.2           | 88.5            |
| Gross revenue                                          | 3,977.8        | 4,736.6         | 4,385.9        | 5,740.7         |
| Cost of merchandise sold                               | 2,851.8        | 3,391.9         | 3,120.8        | 4,082.9         |
| Selling, general and administrative expenses           | 992.6          | 1,075.4         | 1,066.1        | 1,170.7         |
| Interest—net                                           |                |                 |                |                 |
| Debt                                                   | 9.5            | 12.3            | 16.1           | 8.2             |
| Capital leases                                         | 46.5           | 47.0            | 47.4           | 48.1            |
| Income before estimated income taxes                   | 77.4           | 210.0           | 135.5          | 430.8           |
| Estimated income taxes                                 | 33.9           | 93.3            | 55.0           | 184.3           |
| Income from retail operations                          | 43.5           | 116.7           | 80.5           | 246.5           |
| Equity in income of insurance operations               | 1.1            | 1.0             | .9             | 2.1             |
| <b>Net income</b>                                      | <b>\$ 44.6</b> | <b>\$ 117.7</b> | <b>\$ 81.4</b> | <b>\$ 248.6</b> |
| <b>Earnings per common and common equivalent share</b> | <b>\$ .35</b>  | <b>\$ .91</b>   | <b>\$ .63</b>  | <b>\$ 1.91</b>  |

|                                                        | Quarter       |                |                |                 |
|--------------------------------------------------------|---------------|----------------|----------------|-----------------|
|                                                        | First         | Second         | Third          | Fourth          |
| <b>1982</b>                                            |               |                |                |                 |
| Sales                                                  | \$3,600.7     | \$4,152.6      | \$3,882.5      | \$5,136.4       |
| Licensee fees and other income                         | 37.9          | 53.6           | 49.0           | 73.5            |
| Gross revenue                                          | 3,638.6       | 4,206.2        | 3,931.5        | 5,209.9         |
| Cost of merchandise sold                               | 2,625.2       | 3,045.8        | 2,828.8        | 3,798.9         |
| Selling, general and administrative expenses**         | 942.7         | 1,002.3        | 1,001.4        | 1,102.7         |
| Interest—net                                           |               |                |                |                 |
| Debt                                                   | 18.5          | 10.8           | 10.6           | 3.1             |
| Capital leases                                         | 43.1          | 43.8           | 44.3           | 45.3            |
| Income before estimated income taxes                   | 9.1           | 103.5          | 46.4           | 259.9           |
| Estimated income taxes                                 | 4.3           | 43.8           | 17.4           | 96.4            |
| Income from retail operations                          | 4.8           | 59.7           | 29.0           | 163.5           |
| Equity in income of insurance operations               | 1.1           | 1.0            | 1.1            | 1.7             |
| <b>Net income</b>                                      | <b>\$ 5.9</b> | <b>\$ 60.7</b> | <b>\$ 30.1</b> | <b>\$ 165.2</b> |
| <b>Earnings per common and common equivalent share</b> | <b>\$ .06</b> | <b>\$ .48</b>  | <b>\$ .24</b>  | <b>\$ 1.28</b>  |

\*The Consolidated Statements of Income have not been restated prior to the acquisition date of Bishop Buffets, Inc. due to immateriality.

\*\*Includes a \$44.5 charge for store closings, of which \$40.3 is included in the fourth quarter.

Cost of merchandise sold was calculated during each interim period utilizing estimated gross profit rates, including an estimate of inflation in the prices of merchandise purchased during the year. If the results of the physical inventory and the annual rate of inflation determined by using the Bureau of Labor Statistics Department Store Index had been known on a quarterly basis, income before estimated income taxes would have been increased (decreased) as shown:

| (Millions) |        |        |
|------------|--------|--------|
| Quarter    | 1983   | 1982   |
| First      | \$ 2.9 | \$26.5 |
| Second     | 2.4    | 24.7   |
| Third      | 2.4    | 9.5    |
| Fourth     | (7.7)  | (60.7) |

# CORPORATE DATA

## Executive Offices

K mart Corporation  
3100 West Big Beaver Road  
Troy, Michigan 48084  
Telephone (313) 643-1000

## Subsidiaries

Bishop Buffets, Inc.  
Cedar Rapids, Iowa

Furr's Cafeterias, Inc.  
Lubbock, Texas

K mart Apparel Corp.  
North Bergen, New Jersey

K mart Canada Limited  
Brampton, Ontario, Canada

K mart Insurance Services, Inc.  
Dallas, Texas

## Annual Meeting

The Annual Meeting will be held  
Tuesday, May 22, 1984, at 9:00 a.m.,  
at K mart International  
Headquarters,  
3100 West Big Beaver Road  
Troy, Michigan

## Transfer Agents and Registrars

National Bank of Detroit  
Detroit, Michigan

First Interstate Bank of California  
Los Angeles, California

## Form 10-K

A copy of the company's Form 10-K  
annual report for 1983 to the  
Securities and Exchange Commission  
will be furnished without charge  
to any shareholder upon written  
request to:

K mart Corporation  
Financial Reporting Department  
3100 West Big Beaver Road  
Troy, Michigan 48084

# OFFICERS

BERNARD M. FAUBER  
*Chairman of the Board  
and Chief Executive Officer*

SAMUEL G. LEFTWICH  
*President and  
Chief Operating Officer*

ROBERT E. DEWAR  
*Chairman of the Executive  
and Finance Committees*

ROBERT E. BREWER  
*Executive Vice President  
Finance*

NORMAN G. MILLEY  
*Executive Vice President  
Merchandising and Subsidiaries*

GRANT W. MORCK  
*Executive Vice President  
Store Management*

LARRY M. PARKIN  
*Senior Vice President*

FREDERICK M. STEVENS  
*Senior Vice President  
Sales and General Merchandise  
Manager*

BERNARD E. THOMAS  
*Senior Vice President  
Personnel and Management  
Development*

HAROLD E. WILCOX  
*Senior Vice President  
Executive Assistant  
to the President*

EDWARD C. ANDREWS  
*Vice President  
Southern Region*

ROGER E. DAVIS  
*Vice President  
General Counsel and Secretary*

RONALD R. DEJAEGHERE  
*Vice President  
Marketing*

GERALD R. FLETCHER  
*Vice President  
Corporate Information Systems*

JOHN P. JOHNSON  
*Vice President  
Real Estate*

HELEN C. LEFLER  
*Vice President  
and Treasurer*

RICHARD S. MILLER  
*Vice President  
Western Region*

JAMES L. MOSER  
*Vice President  
Merchandise Coordination  
(elected 1/26/84)*

THOMAS H. NIGOLIAN  
*Vice President  
Midwestern Region  
(elected 1/26/84)*

ARTHUR E. RILEY  
*Vice President  
Eastern Region*

HAROLD O. SCARLETT  
*Vice President  
Construction*

MICHAEL L. SKILES  
*Vice President  
Corporate Facilities*

A. ROBERT STEVENSON  
*Vice President  
Government and Public Relations*

JOSEPH R. THOMAS  
*Vice President  
Distribution, Transportation and  
Merchandise Systems*

DAVID P. WALLING  
*Vice President  
Corporate Accounting and  
Reporting*

RICHARD O. WILLIAMS  
*Vice President  
Central Region*

## DIRECTORS



**A. H. AYMOND**  
*Editorial Chairman  
 of the Journal  
 Consulting Power Company*



**WILLIAM H. BALDWIN**  
*Chairman and Director  
 of The Kresge Foundation*



**ROBERT E. BREAKER**  
*Executive Vice President*



**MARY S. COLLATAN**  
*Chairman  
 of the Board  
 of the American  
 Electric Power Association*



**DAIEL R. CORSON**  
*President, University of  
 Cornell University*



**ROBERT E. DEWAR**  
*Chairman of the Executive  
 and Finance Committee*



**BERNARD M. LAUBER**  
*Chairman of the Board*



**CARL A. GERSACKLER**  
*Chairman of the Board  
 of the American  
 Electric Power Association*



**DAVID B. HARPER**  
*President of Con Edison, Inc.*



**SAMUEL C. LEFFWICHT**  
*President*



**EDWARD LUNDY**  
*Editorial Chairman  
 of the Journal  
 of the American  
 Electric Power Association*



**PAUL W. MCCracken**  
*Chairman of the Board  
 of the American  
 Electric Power Association  
 of the American  
 Electric Power Association*



**NORMAN C. MILLEY**  
*Chairman of the Board  
 of the American  
 Electric Power Association*



**GRANT W. MORCK**  
*Chairman of the Board  
 of the American  
 Electric Power Association*



**ROBERT W. PURCELL**  
*Chairman of the Board  
 of the American  
 Electric Power Association*



**GLORIANE SHATTO**  
*Chairman of the Board  
 of the American  
 Electric Power Association*

## COMMITTEES OF THE BOARD

### AUDIT

David B. Harper  
 Paul R. Corson  
 Edward Lundy  
 Gloriane Shatto

### COMPENSATION AND INCENTIVES

Edward Lundy  
 William H. Baldwin  
 Carl A. Gersackler  
 Robert W. Purcell

### EXECUTIVE

Robert E. Dewar  
 A. H. Aymond  
 William H. Baldwin  
 Bernard M. Lauber  
 Carl A. Gersackler  
 Samuel C. Leffwicht

### FINANCE

Robert E. Dewar  
 A. H. Aymond  
 William H. Baldwin  
 Bernard M. Lauber  
 Carl A. Gersackler  
 Samuel C. Leffwicht  
 Edward Lundy  
 Paul W. McCracken  
 Robert W. Purcell

### NOMINATING

Carl A. Gersackler  
 William H. Baldwin  
 Mary S. Collatan  
 Paul W. McCracken  
 Robert W. Purcell

### PUBLIC AFFAIRS

Paul R. Corson  
 Robert E. Dewar  
 David B. Harper  
 Samuel C. Leffwicht  
 Paul W. McCracken  
 Norman C. Milley

## CHANGE IN THE BOARD OF DIRECTORS

Arnold H. Baehner  
 Chairman of the Board  
 of the American  
 Electric Power Association  
 has resigned and will leave  
 the board in December.  
 Harold G. Smith  
 Chairman of the Board  
 of the American  
 Electric Power Association  
 has resigned and will leave  
 the board in December.

BULK RATE  
U.S. POSTAGE

PAID

Fredonia, Wis.  
Permit No. 20

K-MART CORPORATION 3100 WEST BIG BEAVER ROAD TROY, MICHIGAN 48064